Fill

ANNUAL REPORT '68

MESA
PETROLEUM CO.

ANNUAL MEETING OF STOCKHOLDERS

The annual meeting of the stockholders of Mesa Petroleum Co. has been postponed until September 5, 1968. Formal notice of the meeting, together with a proxy statement and a form of proxy is enclosed.

AR15

Preliminary Prospectus dated September 25, 1968

A registration statement relating to these securities has been filed with the Securities and Exchange Commission but has not yet become effective. Information contained herein is subject to completion or amendment. These securities may not be sold nor may offers to buy be accepted prior to the time the registration statement becomes effective. This prospectus shall not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of these securities in any State in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such State.

MESA PETROLEUM CO.

1,711,760 Shares $2.50 Cumulative Convertible Preferred Stock ($1 Par Value)
Each share initially convertible into 1.8 shares of Common Stock

EXCHANGE OFFER TO HOLDERS OF COMMON STOCK OF HUGOTON PRODUCTION COMPANY

Mesa Petroleum Co. (the "Company") hereby offers, on the terms and subject to the conditions set forth herein under "The Exchange Offer," to exchange shares of its $2.50 Cumulative Convertible Preferred Stock ("Preferred Stock") for all of the outstanding shares of common stock ("Hugoton Stock") of Hugoton Production Company ("Hugoton") in the ratio of one share of Preferred Stock for each share of Hugoton Stock tendered.

The Preferred Stock is entitled to one vote per share and cumulative cash dividends at the rate of $2.50 per year. Before March 1, 1974 the Preferred Stock is callable at $85 per share and thereafter at $75 per share. It is convertible into 1.8 shares of the Company's Common Stock until March 1, 1974, and into 1.6 such shares thereafter. The Preferred Stock is entitled to $75 per share on liquidation. Application will be made to list the Preferred Stock on the American Stock Exchange. See "Description of Capital Stock of the Company".

Prior to this offering there have been no outstanding shares of the Company's Preferred Stock. On September 23, 1968 the last sale price of the Company's Common Stock on the American Stock Exchange was $40⅜. See "Comparative Per Share Data".

The Exchange Offer expires on [two weeks after the date of this Prospectus], 1968 unless extended by the Company as provided herein.

The Dealer Managers have agreed to arrange for selected Dealers, including themselves, to solicit acceptances of the Exchange Offer. The Company will pay such Dealers, including the Dealer Managers, a fee of 90¢ for each share of Hugoton Stock tendered where such Dealer is named in the Letter of Transmittal accompanying such shares. The Dealer Managers will be paid a fee of 45¢ for each such share tendered but in no event less than $70,000. See "The Exchange Offer — Procedure for Acceptance". The estimated aggregate maximum amount of expenses of the Exchange Offer, excluding presently indeterminable amounts payable to such Dealers, is $........, all of which will be paid by the Company.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

NEW YORK SECURITIES CO. | **BACON, WHIPPLE & CO.**

The date of this Prospectus is October ...., 1968

No dealer, salesman or any other person has been authorized to give any information or to make any representations, other than those contained in this Prospectus, in connection with the offering contained herein, and, if given or made, such information or representations must not be relied upon as having been authorized by the Company or any other person. This Prospectus does not constitute an offer to exchange or sell, or a solicitation of an offer to exchange or buy, the securities covered by this Prospectus by the Company or any other person in any state or other jurisdiction to any person to whom it is unlawful for the Company or any other person to make such offer or solicitation. Neither the delivery of this Prospectus, nor any exchange or sale made hereunder shall, under any circumstances, create an implication that there has been no change in the facts herein set forth since the date hereof.

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Until ...., 1968 (40 days after the date of this Prospectus), all dealers effecting transactions in the registered securities, whether or not participating in this distribution, may be required to deliver a Prospectus. This is in addition to the obligation of dealers to deliver a Prospectus when acting as underwriters.

IN CONNECTION WITH THIS OFFERING, THE DEALER MANAGERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE PREFERRED STOCK AND OF THE COMMON STOCK OF THE COMPANY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED, IN THE CASE OF THE COMMON STOCK, ON THE AMERICAN STOCK EXCHANGE OR OTHERWISE AND, IN THE CASE OF THE PREFERRED STOCK, ON A WHEN-ISSUED BASIS AND AFTER ISSUANCE IN THE OVER-THE-COUNTER MARKET UNLESS AND UNTIL LISTED ON THE AMERICAN STOCK EXCHANGE AND THEREAFTER ON SUCH EXCHANGE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

THE COMPANY

Mesa Petroleum Co. was organized under the laws of the State of Delaware in February, 1964. It is principally engaged in the evaluation, exploration, development and operation of oil and natural gas properties located primarily in Western Canada, the Anadarko Basin of Texas and Oklahoma and the Rocky Mountains. Within the past year the Company has acquired interests in offshore leases in the Cook Inlet of Alaska and the Santa Barbara Channel of California. Mesa also mines gilsonite in Utah and has minor investments in community antenna television systems and a tract of undeveloped real estate in Texas.

As used herein, the term "Company" refers to Mesa and its consolidated subsidiaries unless the context otherwise requires. The principal offices of the Company are located in Amarillo, Texas, Calgary, Alberta, and Denver, Colorado.

HUGOTON

Hugoton Production Company was incorporated in Delaware on September 22, 1948. Hugoton is engaged in the production and gathering of natural gas from wells located in the Hugoton Field in the State of Kansas and in the sale of such gas solely for use in the State of Kansas. Hugoton also engages in the extraction and sale of natural gasoline and other liquefied products from the gas produced by it.

The Company has requested Hugoton to furnish information about the business, properties, and operations of Hugoton as well as financial statements for inclusion by the Company in this Prospectus and the Registration Statement of which this Prospectus is a part in order that Hugoton stockholders may be fully advised as to the merits of the proposed offering. Hugoton has not yet responded to such request. Consequently, all information and financial material relating to Hugoton is based upon information released publicly by Hugoton or filed by it with the Securities and Exchange Commission ("Commission"). The Commission has not approved or disapproved or passed on the accuracy or adequacy of such material filed with it. The financial statements of Hugoton which appear in this Prospectus are included herein without certification of independent public accountants. See "Source of Financial Statements of Hugoton."

REASONS FOR THE EXCHANGE OFFER

The Company believes that increased benefits to its own and Hugoton's stockholders could be realized in the future by combining Hugoton's assets and operations with those of the Company although there is no assurance that such combination can be accomplished pursuant to this Exchange Offer. Should the Company acquire a substantial number of the outstanding shares of Hugoton Stock, the Company may propose a combination of the two companies by merger, consolidation or otherwise, either on the same terms as this Exchange Offer or on other terms as might be agreed upon by the Company and Hugoton. However, no definite proposals can be made until the result of the Exchange Offer is known. There can be no assurance that the Company will propose such a combination or, if proposed, that the combination will be effected. In any event such a proposal would be subject to approval by the stockholders of Hugoton and, under certain circumstances, approval by the stockholders of the Company.

The Company cannot determine the number of shares of Hugoton Stock which will be tendered, the percentage of voting power to be represented thereby, or the number of shares of the Company's Preferred Stock to be issued therefor. If all shares of Hugoton Stock are tendered, the Company would be required to issue 1,711,760 shares of the Preferred Stock which would be immediately convertible into 3,081,168 shares of the Company's Common Stock.

Stockholders of Hugoton who accept the Exchange Offer will acquire a senior security of the Company, with a preferential dividend of $2.50 per year, which affords them the opportunity to convert such security into the Company's Common Stock.

THE EXCHANGE OFFER

The Company hereby offers to exchange one share of its Preferred Stock for each outstanding share of Hugoton Stock tendered in accordance with this Exchange Offer. All shares of Hugoton Stock properly tendered will be accepted for exchange, subject to the terms and conditions hereinafter set forth.

Tendered Hugoton Stock

All tenders of Hugoton Stock are irrevocable. Transfers of record of tendered stock will not be made before the relevant Effective Date of Exchange. Tendered stock which is not tendered in proper form will be held by the Exchange Agent and a correction letter forwarded to the tendering stockholder. If the tender is not put in proper form within a reasonable time, then the improperly tendered stock will be returned, without cost, by the Exchange Agent to the tendering holder as soon as practicable. Until the relevant Effective Date of Exchange, ownership of tendered shares of Hugoton Stock will remain in the tendering holders unimpaired except for the Company's right to acquire such ownership under the Exchange Offer as of such relevant Effective Date of Exchange. Accordingly, any dividends declared on the Hugoton Stock and payable to holders of record as of a date prior to the relevant Effective Date of Exchange will be paid to the tendering holders.

Expiration Date

Except as provided under the caption "Conditions of the Exchange Offer" below, the Exchange Offer will expire on [two weeks after the date of this Prospectus], 1968, at 5:00 P.M., New York Time, or at that time on any later date to which the Exchange Offer may be extended from time to time by written notice from the Company to the Exchange Agent (the "Expiration Date"). The Company intends to cause notice of any extensions of the Exchange Offer to be published in The Wall Street Journal, The New York Times and other newspapers selected by the Company.

Effective Date of Exchange

As to all shares of Hugoton Stock properly tendered on or prior to the close of business on ...., 1968, the Effective Date of Exchange will be ...., 1968. If the Exchange Offer is extended by the Company, the Effective Date of Exchange in respect of all shares properly tendered after ...., 1968, will be the Monday next following the date on which the shares of Hugoton Stock are tendered.

Procedure for Acceptance

A holder of shares of Hugoton Stock may exchange his shares by filling in and signing the Letter of Transmittal, provided by the Company, the Exchange Agent, the Dealer Managers

and selected Dealers for that purpose, and forwarding the Letter of Transmittal, together with his stock certificates, to the Exchange Agent on or prior to the Expiration Date. **Letters of Transmittal or certificates should not be sent to the Company.** Shares will be deemed timely tendered if (i) a properly executed Letter of Transmittal, accompanied by stock certificates, has been deposited with the Exchange Agent or with a commercial bank or trust company in the continental United States, or with a member firm of the New York or American Stock Exchange or member of the National Association of Securities Dealers, Inc.; (ii) if not deposited with the Exchange Agent, such Agent shall (a) have received from the bank, trust company, firm or member, prior to the Expiration Date, a letter or telegram giving the name of the tendering holder and the number of shares tendered and guaranteeing delivery of the tendered shares (in which case, subject to subsequent compliance with clause (b) below, the shares to which the letter or telegram relates shall be deemed properly tendered as of the date of receipt of the letter or telegram); and (b) thereafter in fact have received the Letter of Transmittal and tendered certificate within eight business days after the relevant Effective Date of Exchange. Any irregularities in connection with the tender of shares must be cured within such time as the Company shall determine, unless waived by the Company in its sole discretion.

The Exchange Agent is Irving Trust Company, One Wall Street, New York, New York 10015.

Delivery of Preferred Stock

Deliveries of the Company's Preferred Stock to exchanging holders will be made as soon as practicable after the relevant Effective Date of Exchange. All deliveries will be made through the Exchange Agent.

Federal Income Tax Status

The exchange will be a taxable disposition by Hugoton stockholders for federal income tax purposes. Consequently each Hugoton stockholder tendering shares of Hugoton Stock will realize taxable gain or loss on the Effective Date of Exchange to the extent that the fair market value of the Company's Preferred Stock received in the exchange is greater or less than such stockholder's income tax basis in the Hugoton Stock so tendered. Provided that such stockholder held his Hugoton Stock as a capital asset, such gain or loss will constitute capital gain or loss determined in accordance with the applicable provisions of the Internal Revenue Code. Such stockholder's income tax basis in the Company's Preferred Stock received in the exchange will be the fair market value thereof on the date of the exchange and the holding period for such stock will commence on such date.

Conditions of the Exchange Offer

Approval by the Company's stockholders of the Exchange Offer is required and is a condition of this offering. The Board of Directors of the Company has unanimously approved the proposed Exchange Offer and has recommended the same be approved by the Company's stockholders at a special meeting of the stockholders to be held ...., 1968. Officers and directors of the Company own in the aggregate approximately 36% of the outstanding Common Stock of the Company and have indicated that they will vote such shares in favor of the Exchange Offer. At the meeting the stockholders will also be presented with a proposal to increase the authorized amount of the Company's Preferred Stock to 5,000,000 shares in order that this Exchange Offer

may be consummated. The affirmative vote of a majority of the votes cast at such meeting is necessary to approve the Exchange Offer, provided that the total vote cast at the meeting represents at least a majority of the shares of the Company's Common Stock entitled to vote at the meeting. The affirmative vote of a majority of the outstanding shares of the Company's Common Stock is required to increase the authorized amount of the Company's Preferred Stock. If approval of both proposals is not obtained, the Exchange Offer will be terminated and all Hugoton Stock theretofore tendered will be returned as soon as practicable.

The Company reserves the right to withdraw or amend its offer at its election at any time prior to the issuance of Preferred Stock to stockholders of Hugoton if (a) in the opinion of the Company, there has occurred any material adverse change in the business or financial condition or material change in the capitalization or number of outstanding shares of Hugoton Stock, or (b) there arises any actual or threatened legal impediment, in the opinion of counsel for the Company, to the acquisition, ownership or voting by the Company of the Hugoton Stock.

Other Purchases

The Company has not at present determined whether it will seek to acquire shares of Hugoton Stock other than the shares to be acquired under this Exchange Offer or whether it will make any subsequent exchange offer to the stockholders of Hugoton for cash, stock, debt or otherwise or recommend a merger or other combination as set forth under "Reasons for the Exchange Offer". The Company reserves the right, in its sole discretion, (a) to make offers subsequent to the expiration of the Exchange Offer for shares of Hugoton Stock on a cash or exchange-of-securities basis, which offers could differ in terms from the Exchange Offer set forth in this Prospectus, or (b) from time to time, to make purchases of securities of Hugoton in the open market or through negotiated purchases, as permitted by the Rules and Regulations of the Securities and Exchange Commission. Under Delaware law, if the Company acquires, under the Exchange Offer or otherwise, at least two-thirds of the outstanding shares of Hugoton Stock, the Company would possess sufficient voting power to cause Hugoton to merge, consolidate or liquidate without concurrence of the remaining Hugoton common stockholders.

Solicitation of Acceptances

Dealer Managers, represented by New York Securities Co. and Bacon, Whipple & Co., have agreed with the Company to use their best efforts to arrange for selected securities dealers ("Dealers"), including themselves, to solicit acceptances of the Exchange Offer. The Company will pay the fees of the Dealer Managers and other Dealers as hereinafter set forth. The Dealer Managers and other Dealers may be deemed to be underwriters within the meaning of the Securities Act of 1933. The Company has agreed to indemnify the Dealer Managers and other Dealers against certain liabilities, including liabilities under the Securities Act of 1933.

The Dealer Managers are to receive a management fee equivalent to 45¢ for each share of Hugoton Stock tendered but in no event less than $70,000. The Dealer Managers may also receive fees as Dealers. A Dealer who has entered into a Soliciting Dealer Agreement with the Dealer Managers and whose name has been inserted by the depositing Hugoton stockholder in a duly executed Letter of Transmittal filed with the Exchange Agent will be entitled to a fee of 90¢ per share for each share of Hugoton Stock tendered.

Payment of Expenses

The expenses to be incurred in connection with the Exchange Offer, including the fees and expenses of the Dealer Managers and of D. F. King & Co. (which has been retained for a fee of $........ plus out-of-pocket expenses to assist in the solicitation of tenders), compensation paid to Dealers, printing, accounting and legal fees, fees for registering the securities offered under Federal and State securities laws, stock transfer taxes, and miscellaneous other items, cannot be estimated with accuracy because of the variable factors involved. Assuming the exchange of all outstanding shares of Hugoton Stock under the Exchange Offer, it is expected that the total expenses, including the above-described fees of the Dealer Managers and other Dealers, will not exceed approximately $........

Transfer Taxes

The Company will pay all transfer taxes applicable to the transfer to it of shares of Hugoton Stock exchanged under the Exchange Offer, except that a tendering holder will bear any taxes which are payable because shares of Preferred Stock are to be issued in a name other than the name in which the Hugoton Stock is registered.

COMPARATIVE PER SHARE DATA

Market Prices

The following table sets forth the range of high and low prices for Common Stock of the Company (and for 1.8 shares of such stock into which each share of Preferred Stock is initially convertible) and the Hugoton Stock for the periods indicated. The prices indicated are bid prices in the over-the-counter market in the case of Hugoton Stock and the Company's Common Stock through September 17, 1967, and sale prices of Common Stock of the Company on the American Stock Exchange after that date. Such over-the-counter quotations represent inter-dealer prices without markup, markdown or commissions and do not represent actual sales. There is no present market for the Preferred Stock as none of such shares is outstanding.

	Company Common Stock		1.8 Shares of Company Common Stock*		Hugoton Common Stock	
Period	High	Low	High	Low	High	Low
1966						
1st Quarter	18¼	10¾	32⅞	19⅜	50¼	43½
2nd Quarter	19¾	14⅞	35½	26¾	54½	40¾
3rd Quarter	14¾	11⅛	26½	20	58½	46½
4th Quarter	14⅛	11⅛	25⅜	20	56½	37
1967						
1st Quarter	20½	12	36⅞	21⅝	45	38¾
2nd Quarter	23⅞	18⅝	43	33½	46¼	43
3rd Quarter	29	20⅜	52¼	36⅝	47	40½
4th Quarter	45¾	26¾	82⅜	48⅛	44¾	40½
1968						
1st Quarter	45¾	34½	82⅜	62⅛	47	40½
2nd Quarter	39¼	33⅝	70⅝	60½	52½	41½
3rd Quarter (through September 23)	43¼	34	77⅞	61¼	63	50

*The conversion rate will be reduced on March 1, 1974 to 1.6 shares of the Company's Common Stock for each share of Preferred Stock.

On September 23, 1968, the closing price for Common Stock of the Company was $40⅜ (equivalent to $72⅝ for 1.8 shares of Common Stock) and the highest reported bid price for Hugoton Stock was $63.

Since July 1, 1968 the Company has purchased an aggregate of 23,800 shares of Hugoton Stock in the open market at a total cost of approximately $1,305,034.

Earnings, Dividends and Stockholders' Equity

The following table sets forth historical and pro forma information as indicated with respect to the Common Stock of the Company and the Hugoton Stock:

	Years Ended April 30,(3)					Pro Forma(1)(2)	
	1964	1965	1966	1967	1968	Before Conversion of Preferred Stock	After Conversion of Preferred Stock
The Company —							
Per common share:							
Income before extraordinary items	—	$ .85	$1.18	$1.56	$1.83		$ 1.58(4)
Extraordinary items	—	—	—	—	—		.18(4)
Net income	—	$ .85	$1.18	$1.56	$1.83		$ 1.76(4)
Dividends	—	.04	.08	.08	.09	.10(5)	.10(5)
Stockholders' equity					11.88	— (8)	5.46(4)
	Years Ended December 31,						
	1963	1964	1965	1966	1967		
Hugoton — Per common share:							
Income before extraordinary items	$2.03	$2.03	$2.13	$2.23	$2.51		$ 2.85(7)
Extraordinary items	—	—	—	—	.19		.32(7)
Net income	$2.03	$2.03	$2.13	$2.23	$2.70		$ 3.17(7)
Dividends	2.00	2.50	2.50	2.00	2.00	2.50(6)	.18(7)
Stockholders' equity					7.20	12.55(8)	9.83(7)

(1) Assumes 100% ownership of Hugoton after this Exchange Offer.
(2) Combines, on a pooling of interests basis, the Company for the year ended April 30, 1968 with Hugoton for the year ended December 31, 1967.
(3) Adjusted to reflect a 10% stock dividend in March, 1967 and a 10% stock dividend in January, 1968.
(4) Assumes conversion of all $2.50 Cumulative Convertible Preferred Stock issued in connection with exchange of Hugoton common stock.
(5) The Company has paid semi-annual cash dividends of $.05 per share since December, 1964.
(6) Represents dividend on $2.50 Cumulative Convertible Preferred Stock of the Company.
(7) Represents amounts relating to 1.8 shares of the Company.
(8) The liquidating preference of the $2.50 Cumulative Convertible Preferred Stock of the Company is $75 per share, or an aggregate of $126,597,000, which is in excess of the pro forma combined stockholders' investment of the Company and Hugoton.

CAPITALIZATION OF THE COMPANY

The following table sets forth the capitalization of the Company as of September 17, 1968, and as adjusted to give effect to the proposed issuance of the Preferred Stock described herein.

	Outstanding	As Adjusted
5½% Convertible Subordinated Debentures due 1983	$6,500,000	$6,500,000
Sundry indebtedness	28,912	28,912
Preferred Stock, $1 par value, authorized 5,000,000 shares	None	1,687,960 shs.(1)
Common Stock, $1 par value, authorized 5,000,000 shares	798,659 shs.(2)	798,659 shs.(2)

(1) Assumes issuance of Preferred Stock for all outstanding shares of Hugoton Stock, except for 23,800 shares of Hugoton Stock owned by the Company, and amendment of the Company's Certificate of Incorporation to increase the authorized Preferred Stock to 5,000,000 shares.

(2) Excludes 34,651 shares reserved for employee stock options, 144,444 shares reserved for conversion of the Company's 5½% Convertible Subordinated Debentures due 1983, and 3,081,168 shares reserved for conversion of the $2.50 Cumulative Convertible Preferred Stock.

The Company has no material obligations under leases on real property.

CONSOLIDATED STATEMENTS OF INCOME OF THE COMPANY

The following consolidated statements of income of the Company and subsidiaries for the four years ended April 30, 1968, have been examined by Arthur Andersen & Co., independent public accountants, as set forth in their report included elsewhere in this Prospectus. The consolidated statements of income for the three-month periods ended July 31, 1967, and 1968, not examined by independent public accountants, reflect, in the opinion of the Company, all adjustments (which included only normal recurring adjustments) necessary to present fairly the results for such periods. These statements should be read in conjunction with the notes to these statements and with the consolidated financial statements and notes thereto included elsewhere in this Prospectus.

	Year Ended April 30				Three Months Ended July 31 (Unaudited)	
	1965	1966	1967	1968	1967	1968
Revenues:						
Oil and gas sales	$1,030,322	$ 856,090	$1,022,865	$1,248,278	$ 269,450	$ 316,171
Proceeds from drilling arrangements and sales of oil and gas leases held for resale	1,138,000	2,308,708	3,836,840	4,494,652	940,776	781,266
Gilsonite sales	—	133,214	320,576	365,302	82,074	103,846
Other operating income	33,096	60,424	88,527	79,593	24,181	111,555
	$2,201,418	$3,358,436	$5,268,808	$6,187,825	$1,316,481	$1,312,838
Expenses:						
Lease operating expenses	$ 319,926	$ 253,797	$ 255,485	$ 321,660	$ 58,893	$ 60,828
Cost of drilling arrangements and sales of oil and gas leases held for resale	695,086	1,417,851	2,555,367	2,859,585	642,882	485,365
Cost of gilsonite sales	—	138,862	271,520	291,719	72,015	76,756
Other operating expenses	28,931	57,906	113,540	74,416	15,391	21,367
General and administrative	272,965	351,110	480,876	606,176	151,318	184,620
Interest	105,958	126,750	194,903	135,159	54,125	52,275
Depreciation, depletion and amortization (Note C)	343,242	305,600	389,447	509,355	120,000	150,000
	$1,766,108	$2,651,876	$4,261,138	$4,798,070	$1,114,624	$1,031,211
Income before extraordinary gain	$ 435,310	$ 706,560	$1,007,670	$1,389,755	$ 201,857	$ 281,627
Extraordinary gain on sale of marketable securities (net of applicable income taxes of $69,958)	—	—	—	—	—	62,539
Net Income (Note D)	$ 435,310	$ 706,560	$1,007,670	$1,389,755	$ 201,857	$ 344,166
Per share of Common Stock (Note A)						
Income before extraordinary gain	$ .85	$1.18	$1.56	$1.83	$ .31	$ .35
Extraordinary gain	—	—	—	—	—	.08
Net income	$ .85	$1.18	$1.56	$1.83	$ .31	$ .43
Cash Dividends Per Share (Note A)	$ .04	$ .08	$ .08	$ .09	$ .04	$ .05

(A) Net income and cash dividends per share are based on the average number of shares outstanding during each period, adjusted for a 10% stock dividend in March, 1967, and a 10% stock dividend in January, 1968 and assuming for the year ending April 30, 1968 that $3,979,000 of the $4,000,000 of 5¾% Convertible Debentures issued on August 2, 1967 were converted into 152,817 shares of common stock as of August 2, 1967. These Debentures were called for redemption on January 12, 1968 and the holders thereof exercised their option and exchanged $3,979,000 principal amount of Debentures for 152,817 shares of common stock. The remaining $21,000 of Debentures were redeemed by the Company. In its annual report for the year ended April 30, 1968, the Company reported earnings per share of $1.98 which amount was based on treating these 152,817 shares of common stock as outstanding from the date the Debentures were called for redemption which method of calculation is permitted under Opinion No. 9 of the Accounting Principles Board.

(B) The Company was organized in February, 1964, and began operations on May 1, 1964, when it acquired in a tax-free exchange (a) all of the outstanding shares of capital stock of Petroleum Exploration, Inc. of Texas and Altair Oil & Gas Co. in exchange for 219,236 shares of common stock, and (b) certain interests in oil and gas properties in exchange for 289,025 shares of common stock. See Note (F).

(Continued on next page)

In September, 1965, the Company acquired substantially all of the assets and assumed the stated liabilities of Standard Gilsonite Company in exchange for 121,000 shares of common stock. The operations of this division have been included in the accompanying statements for the period from the date of acquisition.

See notes 2 and 3 to the consolidated financial statements for further details pertaining to organization and acquisitions.

(C) The Company follows the accounting policy of capitalizing for financial reporting purposes all direct costs incurred in the acquisition, exploration, and development of gas and oil reserves, including nonproductive costs. Such capitalized costs are being amortized on a company-wide composite unit-of-production method over the aggregate productive life of all of its producing oil and gas properties. Under this method of accounting, no gains or losses are recognized upon sale or disposition of oil and gas properties, except in extraordinary transactions. Through July 31, 1968, nonproductive costs capitalized, net of gains on sales of producing properties which have been credited to property, amounted to approximately $1,675,000.

(D) Because of the deductibility for tax purposes of amounts capitalized and amortized for financial reporting purposes, no provision for Federal or Canadian income taxes during any of the four years ended April 30, 1968, has been necessary. To date, the Company has received no Federal income tax benefits from nonproductive well costs capitalized for financial reporting purposes.

As of July 31, 1968, the Company has estimated unused operating loss carry-forwards of $1,250,000 which are available to reduce or eliminate Federal income taxes which may be payable in future periods. These losses, if not utilized, will expire by 1973.

(E) The Company has two contributory profit sharing plans. Reference should be made to the subcaption "Remuneration" under the caption "Management of the Company" elsewhere in the Prospectus for further particulars.

(F) The following is a summary of the combined results of operations of Petroleum Exploration, Inc. of Texas and Altair Oil & Gas Co. for the two periods prior to acquisition, May 1, 1964, by the Company as described in Note (B). Approximately forty-three percent of the total shares issued by the Company on May 1, 1964, was issued for the stock of these two companies and approximately fifty-seven percent was issued for certain interests in oil and gas properties as described in Note (B). The summary below does not include the results of operations for the respective periods applicable to these interests in oil and gas properties because such information is not available. The oil and gas sales of the Company subsequent to April 30, 1964, reflect the operations of these acquired properties. Revenues from drilling arrangements and sales of oil and gas leases of the Company are a continuation of similar activities previously conducted by Petroleum Exploration, Inc. of Texas and Altair Oil & Gas Co.

	(Unaudited)	
	Period Ending(1) In 1963	Period Ending April 30, 1964(2)
Revenues:		
Oil and gas sales	$ 383,421	$ 193,243
Drilling arrangements and sales of oil and gas leases held for resale	1,114,907	1,100,068
Other operating income	—	17,828
	$1,498,328	$1,311,139
Expenses:		
Lease operating expenses	$ 102,015	$ 57,894
Cost of drilling arrangements and sales of oil and gas leases held for resale	846,918	709,321
Dry hole and other exploratory costs(3)	84,320	127,011
Other operating expenses	—	15,788
General and administrative	184,969	125,023
Interest	75,309	63,670
Depreciation, depletion and amortization	205,071	110,655
Provision (credit) for deferred Federal income tax(4)	(50,000)	(13,000)
	$1,448,602	$1,196,362
Net Income	$ 49,726	$ 114,777

(1) Combines the fiscal years ended August 31 for Petroleum Exploration, Inc. of Texas and May 31 for Altair Oil & Gas Co.

(2) Combines the eight months ended April 30 for Petroleum Exploration, Inc. of Texas and the eleven months ended April 30 for Altair Oil & Gas Co.

(3) The companies followed the policy of capitalizing all costs related to productive oil and gas wells and undeveloped leases and of charging to expense as incurred all costs of nonproductive exploration and wells.

(4) The credits for deferred Federal income taxes applicable to the operations of the predecessor companies represent the taxes which would have been refundable during the applicable periods, if these companies had followed the accrual basis of accounting for Federal income tax purposes rather than the cash basis of accounting.

STATEMENTS OF INCOME OF HUGOTON

The following statements of income of Hugoton have been taken from Hugoton's annual and quarterly reports and from reports filed with the Securities and Exchange Commission, as set forth under "Source of Financial Statements of Hugoton." The Commission does not approve or disapprove or pass on the accuracy or adequacy of financial statements or of other information filed with it. The statements should be read in conjunction with the other financial statements of Hugoton and related notes appearing elsewhere in this Prospectus.

	Year Ended December 31					Six Months Ended June 30	
	1963	1964	1965	1966	1967	1967	1968
Operating revenues:							
Natural gas	$6,140,777	$7,109,078	$7,042,395	$7,432,574	$8,263,888	$4,345,943	$4,650,917
Products extracted from natural gas	894,059	893,398	1,091,630	1,252,993	1,446,815	722,464	879,475
Revenue from gas processed by others	—	—	—	—	106,373	46,955	—
Total operating revenues	7,034,836	8,002,476	8,134,025	8,685,567	9,817,076	5,115,362	5,530,392
Operating expenses and taxes:							
Gas purchased	30,659	48,441	42,951	10,787	12,823		
Gas royalties	736,462	803,103	931,662	1,024,880	1,114,139		
Non-productive well drilling	145,183	—	—	—	—		
General and administrative expenses	349,881	408,205	364,206	480,318	449,058	1,044,267	1,038,531
Other operating expenses	327,594	357,773	363,418	380,155	427,463		
Maintenance	42,355	32,568	38,946	46,232	36,248		
Provision for depreciation, depletion and amortization	307,935	335,946	332,052	382,319	524,917	221,739	306,240
State, local and miscellaneous Federal taxes	169,070	188,128	169,227	202,319	302,612	180,754	237,029
Provision for income taxes:							
Federal income taxes (a)	1,541,000	2,415,000	2,296,000	2,435,000	2,712,000	1,463,000	1,764,000
State income taxes	51,000	70,000	114,000	126,000	141,000		
Total operating expenses and taxes	3,701,139	4,659,164	4,652,462	5,088,010	5,720,260	2,909,760	3,345,800
Operating income	3,333,697	3,343,312	3,481,563	3,597,557	4,096,816	2,205,602	2,184,592
Other income (deductions):							
Dividends received	35,170	44,950	82,092	86,602	62,288		
Interest revenue	89,576	80,190	68,047	133,564	137,849		
Oil and gas well royalties	3,446	2,170	2,536	2,351	1,548	117,436	124,444
Gain (Loss) on sale of investments	—	—	—	725	7,500		
Total other income	128,192	127,310	152,675	223,242	209,185	117,436	124,444
Income before extraordinary item	3,461,889	3,470,622	3,634,238	3,820,799	4,306,001	2,323,038	2,309,036
Extraordinary item — gain on disposition of investment securities, net of income tax of $101,015	—	—	—	—	319,879	319,879	—
Net income	$3,461,889	$3,470,622	$3,634,238	$3,820,799	$4,625,880	$2,642,917	$2,309,036
Earnings per share (based on outstanding shares at end of year):							
Income before extraordinary item	$2.03	$2.03	$2.13	$2.23	$2.51	$1.35	$1.35
Extraordinary item	—	—	—	—	.19	.19	—
Net income	$2.03	$2.03	$2.13	$2.23	$2.70	$1.54	$1.35
Cash dividends per share	$2.00	$2.50	$2.50	$2.00	$2.00	$1.00	$1.00

Notes — See next page.

NOTES:

(a) On April 20, 1966, the Internal Revenue Service proposed deficiencies in Hugoton's Federal income taxes for the years 1958-1964 in the amount of $1,843,045, which, with interest (net of taxes), would approximate $2,150,000. The proposed deficiencies are based primarily on a recomputation of the depletion deduction under the method employed by the Court of Claims in its 1965 decision relating to Hugoton's Federal income tax liability for the years 1952-1957. A protest has been lodged against the proposed deficiencies and the matter is now pending before the Appellate Division of the Regional Commissioner's Office at Wichita, Kansas.

A settlement offer of $1,140,000, exclusive of interest, has been made to the Appellate Division covering all years through 1964. The offer has been recommended for acceptance by the Appellate Conferee, with the final acceptance subject to review and approval by the Appellate Division Review, at Oklahoma City, Oklahoma. As of the current date, the settlement offer is pending.

Although it is not possible to determine the ultimate liability for such years until the various issues are resolved, provision was made retroactively, during 1966, for estimated additional income taxes (plus interest, net of taxes) for the years 1958-1964 in the amount of $1,500,000. Additionally, since any settlement of the proposed deficiencies for such years may also be applicable to subsequent years, the provisions for Federal income taxes for the years 1965-1967 have been made on a basis consistent with the assumptions used in recording the estimated additional liability for prior years.

Should the position of the Internal Revenue Service ultimately prevail for the period 1958-1964 and subsequent years, an additional liability (including interest, net of taxes) estimated to approximate $800,000 would be incurred.

Hugoton has had the benefit for Federal income tax purposes of certain deductions such as intangible development costs, which have not been written off on the books. The investment tax credit (of immaterial amount) has been reflected as a reduction of the provision for Federal income taxes.

The provision for Federal income taxes is affected by certain factors which cannot be definitely determined until the close of the calendar year; thus, the income statements for the six-month periods ended June 30, 1967 and 1968 cannot always reflect the tax expense finally applicable to such periods.

(b) Under a proceeding with the Federal Power Commission, Hugoton is seeking to obtain authorization for the abandonment of a sale of natural gas to Panhandle Eastern Pipe Line Company. An Examiner's decision in this matter was issued on November 24, 1967 denying the application and ordering Hugoton to make refunds (with interest) of alleged excess charges for the years 1956-1965. Should the Examiner's decision be affirmed by the Commission, it is estimated that the maximum amount of the refund that would be required (with interest), net of taxes, will approximate $1,100,000.

Hugoton disputes the legality of the Examiner's decision but has recently filed a settlement proposal with the Commission. This proposal would accept the denial of the abandonment and would provide for a refund of approximately $250,000 (with interest), net of taxes, which amount has been charged to retained earnings in the accompanying financial statements. If the settlement proposal is rejected by the Commission, Hugoton will have the opportunity to appeal the Examiner's decision.

(c) Hugoton has a pension plan covering substantially all of its employees. The total pension expense for the years 1963, 1964, 1965, 1966 and 1967 was $33,613, $44,424, $46,677, $49,099 and $52,071, respectively. The plan is fully funded through insurance.

The plan is non-contributory and may be terminated at the option of Hugoton. It provides for the retirement of employees (including officers) at age 65 with annuity payments based on length of service.

PRO FORMA STATEMENTS OF INCOME OF THE COMPANY AND HUGOTON

(Unaudited)

The following pro forma condensed statements of income, which combine, on a pooling of interests basis, the consolidated statements of the Company for the year ended April 30, 1968 with that of Hugoton for the year ended December 31, 1967 (prepared from the annual report to stockholders), give effect to the assumptions that the Company, after this Exchange Offer, will (on the basis of Hugoton shares outstanding on December 31, 1967) own (1) 80% and (2) 100% of the outstanding common stock of Hugoton.

				80%		100%	
	Company	Hugoton	Combined	Adjustments	Pro Forma	Adjustments	Pro Forma
Revenues:							
Oil and gas sales	$ 1,248,278	$ 8,263,888	$ 9,512,166		$ 9,512,166		$ 9,512,166
Proceeds from drilling arrangements and sales of oil and gas leases held for resale	4,494,652	—	4,494,652		4,494,652		4,494,652
Products extracted from natural gas	—	1,446,815	1,446,815		1,446,815		1,446,815
Other	444,895	315,558	760,453		760,453		760,453
	$ 6,187,825	$10,026,261	$16,214,086	$ —	$16,214,086	$ —	$16,214,086
Expenses:							
Cost of drilling arrangements and sales of oil and gas leases held for resale	$ 2,859,585	$ —	$ 2,859,585		$ 2,859,585		$ 2,859,585
Operating expenses	687,795	2,034,285	2,722,080		2,722,080		2,722,080
General and administrative	606,176	449,058	1,055,234		1,055,234		1,055,234
Interest	135,159	—	135,159		135,159		135,159
Depreciation, depletion and amortization	509,355	524,917	1,034,272		1,034,272		1,034,272
Provision for Federal income taxes	—	2,712,000	2,712,000	$ (309,000) (a)	2,403,000	$ (309,000) (a)	2,403,000
Minority interest in net income of Hugoton	—	—	—	925,176 (b)	925,176		—
	$ 4,798,070	$ 5,720,260	$10,518,330	$ 616,176	$11,134,506	$ (309,000)	$10,209,330

Income before Extraordinary Items	$ 1,389,755	$ 4,306,001	$ 5,695,756	$ (616,176)	$ 5,079,580	$ 309,000	$ 6,004,756
Extraordinary Items —							
Gain on disposition of investment securities, net of income tax of $101,015	$ —	$ 319,879	$ 319,879		$ 319,879		$ 319,879
Utilization of Federal income tax loss carry forward	—	—	—	$ 363,000 (a)	363,000	$ 363,000 (a)	363,000
	$ —	$ 319,879	$ 319,879	$ 363,000	$ 682,879	$ 363,000	$ 682,879
Net Income	$ 1,389,755	$ 4,625,880	$ 6,015,635	$ (253,176)	$ 5,762,459	$ 672,000	$ 6,687,635
PRO FORMA EARNINGS PER SHARE on average shares of common stock outstanding assuming conversion of $2.50 cumulative convertible preferred stock —							
Net income before extraordinary items					$1.59		$1.58
Extraordinary items .					.21		.18
Net income					$1.80		$1.76

Pro forma adjustments:

(a) To give effect to the reduction in Federal income tax expense for the year ended April 30, 1968, due to the company's tax operating loss for that period of $643,000 and tax loss carry forward as of the beginning of that period of $757,000, which tax losses could have been utilized by the combined company. The tax benefit of the loss carry forward has been shown as an extraordinary item.

(b) To set out the 20 percent minority interest in Hugoton under the assumption that only 80 percent of Hugoton shares are acquired.

PRO FORMA BALANCE SHEETS OF THE COMPANY AND HUGOTON

(Unaudited)

The following pro forma condensed balance sheets, which combine on a pooling of interests basis, the consolidated balance sheet of the Company as of April 30, 1968 with that of Hugoton as of December 31, 1967 (prepared from the annual report to stockholders), give effect to the assumptions that the Company, after this Exchange Offer, will (on the basis of Hugoton shares outstanding on December 31, 1967) own (1) 80% and (2) 100% of the outstanding common stock of Hugoton.

				80%		100%	
	Company	Hugoton	Combined	Adjustments	Pro Forma	Adjustments	Pro Forma
ASSETS							
Current Assets:							
Cash	$ 552,818	$ 1,487,355	$ 2,040,173	$2,352,500 (a) (1,305,034) (b)	$ 3,087,639	$2,352,500 (a) (1,305,034) (b)	$ 3,087,639
Marketable securities	—	2,098,906	2,098,906		2,098,906		2,098,906
Accounts receivable	2,303,492	952,720	3,256,212		3,256,212		3,256,212
Inventories:							
Oil and gas leases held for resale within one year	1,234,924	—	1,234,924		1,234,924		1,234,924
Other	37,548	103,948	141,496		141,496		141,496
Prepayments	33,453	6,772	40,225		40,225		40,225
Total current assets	$ 4,162,235	$ 4,649,701	$ 8,811,936	$1,047,466	$ 9,859,402	$1,047,466	$ 9,859,402
Investments, at cost	572,341	773,855	1,346,196	1,305,034 (b) (1,305,034) (c)	1,346,196	1,305,034 (b) (1,305,034) (c)	1,346,196
Property, Plant and Equipment, at cost	11,207,898	14,471,646	25,679,544		25,679,544		25,679,544
Less — Accumulated depreciation, depletion and amortization	(1,591,926)	(4,720,027)	(6,311,953)		(6,311,953)		(6,311,953)
Deferred Charges and Other Assets:							
Deferred debt discount and expense	—	—	—	287,500 (a)	287,500	287,500 (a)	287,500
Other	175,465	—	175,465		175,465		175,465
	$14,526,013	$15,175,175	$29,701,188	$1,334,966	$31,036,154	$1,334,966	$31,036,154
LIABILITIES							
Current Liabilities:							
Current maturities on long-term debt	$ 11,500	$ —	$ 11,500		$ 11,500		$ 11,500
Accounts payable and accrued liabilities	925,761	279,635	1,205,396		1,205,396		1,205,396
Accrued Federal income taxes	—	2,321,748	2,321,748	$ (672,000) (e)	1,649,748	$ (672,000) (e)	1,649,748
Reserve for possible refund, net	—	250,000	250,000		250,000		250,000
Total current liabilities	$ 937,261	$ 2,851,383	$ 3,788,644	$ (672,000)	$ 3,116,644	$ (672,000)	$ 3,116,644

Long-Term Debt, net of current maturities	3,880,465	—	3,880,465	(3,880,000) (a) 6,500,000 (a)	6,520,465	(3,880,000) (a) 6,500,000 (a)	6,520,465
Deferred Income from Sale of Production Payment	220,105	—	220,105		220,105		220,105
Minority Interest in Hugoton	—	—	—	2,464,759 (d)	2,464,759		—
Total liabilities	$ 5,037,831	$ 2,851,383	$ 7,889,214	$4,432,759	$12,321,973	$1,968,000	$ 9,857,214
Stockholders' Investment:							
$2.50 Cumulative convertible preferred stock, $1 par (liquidating preference of $100,920,600 assuming 80% ownership of Hugoton common stock and $126,597,000 assuming 100% ownership of Hugoton common stock				$1,345,608 (f)	$ 1,345,608	$1,687,960 (f)	$ 1,687,960
Common stock	$ 798,659	$ 1,711,760	$ 2,510,419	(1,345,608) (f) (342,352) (d) (23,800) (c)	798,659	(1,687,960) (f) (23,800) (c)	798,659
Capital surplus	7,835,556	318,839	8,154,395	(4,427) (c) (63,768) (d)	8,086,200	(4,427) (c)	8,149,968
Reinvested earnings	853,967	10,293,193	11,147,160	(1,276,807) (c) (2,058,639) (d) 672,000 (e)	8,483,714	(1,276,807) (c) 672,000 (e)	10,542,353
Total stockholders' investment	$ 9,488,182	$12,323,792	$21,811,974	$(3,097,793)	18,714,181	$ (633,034)	$21,178,940
	$14,526,013	$15,175,175	$29,701,188	$1,334,966	$31,036,154	$1,334,966	$31,036,154

Pro forma adjustments:

(a) To give effect to the issuance of $6,500,000 of 5½% convertible subordinated debentures due 1983, which were issued by the Company on September 13, 1968.

(b) To give effect to the purchase of 23,800 shares of Hugoton common stock by the Company during the months of July, August, and September, 1968.

(c) To give effect to the elimination of the Company's investment in Hugoton, as set forth in (b) above.

(d) To set out the 20 percent minority interest in Hugoton under the assumption that only 80 percent of Hugoton shares are acquired.

(e) To give effect to the reduction in Federal income tax payable, as set forth in pro forma adjustment (a) to the pro forma statements of income of the Company and Hugoton.

(f) To give effect to the issuance of $2.50 cumulative convertible preferred stock, $1 par value.

BUSINESS AND PROPERTY OF THE COMPANY

As of May 1, 1964, the Company acquired, in exchange for shares of its Common Stock, certain producing oil and gas properties and all of the outstanding capital stock of Petroleum Exploration, Inc. of Texas ("PEI") and Altair Oil & Gas Co. ("Altair"). PEI was organized in 1956 to engage in oil and gas exploration and drilling activities in Texas and Oklahoma for its own account and in participation with others. The management and stockholders of PEI organized Altair in 1959 to conduct similar activities in Western Canada. As a result of their joint drilling operations with others, most of the oil and gas properties in which PEI and Altair owned interests were also owned in part by several other participants. Upon consummation of the Company's exchange offer, these corporations became wholly owned subsidiaries, and the Company acquired the outstanding fractional interests of certain of such participants. An aggregate of 508,261 shares of the Company's Common Stock was issued pursuant to the exchange offer. PEI and Altair continued to operate as subsidiaries of the Company until April 30, 1967, when they were merged into it.

In September, 1965, the Company acquired substantially all the assets of Standard Gilsonite Company, which owned gilsonite reserves and a crushing mill and storage and bagging facilities in Utah, in exchange for 121,000 shares of Common Stock and the assumption of Standard's liabilities. The Company also has minor investments in community antenna television systems and a tract of undeveloped real estate in Texas.

Oil and Gas Operations

Method of Operation

The oil and gas operations of the Company consist of the geological and geophysical evaluation of prospective oil and gas properties, the acquisition of leases or other interests in promising prospects, the drilling of one or more exploratory test wells on such prospects and the development and operation of those properties having potentially profitable reserves. The Company maintains offices in Amarillo, Texas; Calgary, Alberta; and Denver, Colorado.

Since its organization, the Company has followed an active lease acquisition program. In order to reduce its heavy investment in lease inventory, to spread the risk involved in drilling expensive test wells (due to remoteness or depth) and to obtain the benefits of geographic diversification by operating in several different areas, the Company generally conducts its oil and gas operations in participation with others, usually on a "turnkey" basis. Under the turnkey arrangement, the Company sells a portion of the working interest in a lease theretofore acquired by it to a third party and agrees to drill an exploratory well to casing point on such lease, all in exchange for a fixed fee. A well has been drilled to casing point when the operator terminates drilling operations and decides whether the well should be abandoned or completion activities undertaken. The fixed fee constitutes the purchaser's total initial investment in the lease and the exploratory well to be drilled thereon. Thus, the Company assumes and relieves the purchaser of any risk in connection with the actual cost of drilling the exploratory well. If such a well is completed as a producer, completion costs, as well as the cost of any additional development wells, are paid by each owner, including the Company, in proportion to his or its ownership of the working interest. Occasionally the Company employs alternative drilling arrangements whereby the cost of both test and development wells is shared pro rata by the owners of the working interest. Regardless of the type of arrangement, the Company retains a percentage of the working interest. During the four-year period ended April 30, 1968, the interest retained by the Company averaged 27%.

The Company owns no drilling rigs and all drilling is done by independent drilling contractors on a bid basis.

Production

The following table summarizes the oil and gas production of the Company, in barrels (Bbls.) of oil (including condensate) and thousands of cubic feet (Mcf) of gas, for the four years ended April 30, 1968:

	1965	1966	1967	1968
Net Crude Oil Produced (Bbls.)	278,592*	214,920*	251,720*	328,767*
Daily Average	763	589	690	901
Net Natural Gas Produced (Mcf)	2,215,392*	2,073,756*	3,187,497*	3,690,697*
Daily Average	6,070	5,681	8,733	10,111
Average Prices for Production				
Oil — Posted field price per Bbl.	$2.57	$2.65	$2.43	$2.19
Gas — Sales price per Mcf	$ .12	$ .14	$ .13	$ .14
Wells Owned				
Gross:				
Oil	219	145	131	153
Gas	59	59	68	77
Shut-in** (16 gas, 1 oil for 1968)	—	11	13	17
Total	278	215	212	247
Net:				
Oil	118.4	63.7	56.8	71.0
Gas	21.0	18.8	20.7	21.9
Shut-in** (2.3 gas, 0.3 oil for 1968)	—	2.8	2.5	2.6
Total	139.4	85.3	80.0	95.5

* Net of interests of others but including for the 1967 fiscal year 52,960 Bbls. and 743,800 Mcf attributable to production payments sold to others and for the 1968 fiscal year 28,395 Bbls. and 746,407 Mcf attributable to production payments sold to others.

** Gas wells awaiting pipeline connection and oil well to be reworked.

As used in this Prospectus, the term "gross wells" means the total number of wells in which the Company has a working interest and the term "net wells" means the number of gross wells multiplied by the percentage of the working interest therein owned by the Company. "Gross acreage" and "net acreage" are computed similarly.

Average daily oil production net to the Company's interest during the months of May, 1965, 1966, 1967 and 1968 were approximately 615, 649, 907 and 1,038 barrels, respectively, for an average daily production per well of approximately 7, 19, 32 and 24 barrels.

The oil produced from the Company's wells in the Hoosier Field in Saskatchewan is below average API gravity. Such oil is 18 gravity and is sold at the posted field price of $1.77 per barrel. Approximately 61% of the Company's total net proved oil and condensate reserves are attributable to the Hoosier Field, but none of the Company's natural gas reserves are located in the Hoosier Field. Approximately 38.8% of the Company's total production of oil and condensate for fiscal 1968 was attributable to the Hoosier Field, compared with approximately 13.7% for fiscal 1967.

Such relative increase in production from the Hoosier Field was the principal cause of the decline in 1968 of the average posted field price per barrel of oil and condensate as shown in the table on the preceding page.

The Company's ownership of oil and gas leases held by production at April 30, 1968, may be summarized as follows:

	Producing Acreage		Producing Wells*			
	Gross	Net	Gross		Net	
Location			Oil	Gas	Oil	Gas
Alberta	2,080	718	8	2	3.6	.3
British Columbia	6,000	1,404	—	4	—	.8
Ontario	600	60	—	2	—	.2
Saskatchewan	9,120	3,555	51	6	19.3	1.2
Kansas	2,566	1,601	60	5	36.9	1.7
Montana	3,039	483	—	7	—	1.1
Oklahoma	15,139	4,672	15	26	4.0	5.5
Texas	21,779	9,112	16	40	6.8	13.1
Wyoming	1,553	403	4	1	.7	.3
Total	61,876	22,008	154	93	71.3	24.2

* Includes gas wells awaiting pipeline connection and oil well to be reworked.

Reserves

A study of the oil and gas reserves of the Company has been made by DeGolyer and MacNaughton, petroleum engineers, as of May 1, 1968. The following letter summarizes such reserve study:

DeGOLYER and MacNAUGHTON
5625 Daniels Avenue
Dallas, Texas

May 22, 1968

Mesa Petroleum Co.
Alta Building
Amarillo, Texas 79105

Gentlemen:

Pursuant to your request we have made an investigation, as of May 1, 1968, of the oil and gas reserves of Mesa Petroleum Co., hereinafter referred to as the "Company." These reserves are located in the states of Kansas, Montana, Oklahoma, Texas, and Wyoming and in Canada.

We have been acquainted generally with the operations of the Company for a period of years. During this investigation, we consulted freely with officers and employees of the Company and were provided access to such accounts, records, geological and engineering reports, and other data as were desired for examination. This report is based upon the data furnished during this investigation and our previous investigation of the subject properties and upon our studies of other properties in many of the fields in which the Company's reserves are located. It was not considered necessary to make a field examination of the physical condition and operation of the properties in which the Company owns interests. Titles to properties, the extent and character of ownership, and all other factual data furnished by the Company were accepted as represented.

We estimate, as of May 1, 1968, the total net proved reserves of the Company to be 3,321,191 barrels of oil and condensate, and 62,631,885 thousand cubic feet of natural gas. All of the gas reserves and approximately 90 percent of the oil and condensate reserves are for properties considered to be developed by the present wells.

Gas reserves were calculated at 14.65 pounds per square inch absolute pressure and 60 degrees Fahrenheit temperature.

We estimate, as of May 1, 1968, that approximately 23 percent of the net proved oil and condensate reserves and 56 percent of the net proved gas reserves of the Company are located in the United States.

During the past two years the Company has been very active in purchasing leasehold interests in approximately 1,500,000 acres in Canada and the United States. These lands are located in favorable geological provinces in the general area of oil and gas producing fields.

Submitted,

DeGOLYER and MacNAUGHTON

Drilling Activity

The following tabulation sets forth the number of wells drilled by or on behalf of the Company (all of which were drilled in conjunction with others) and the results thereof for the four years ended April 30, 1968:

	1965	1966	1967	1968
Gross Wells				
Exploratory:				
Dry	14	8	28	29
Producing	4	7	6	8
Semi-proven:				
Dry	5	10	14	11
Producing	13	17	12	11
Proven:				
Dry	0	0	0	5
Producing	10	5	17	10
Grand Total	46	47	77	74
Net Wells				
Exploratory:				
Dry	3.6	2.0	7.0	8.2
Producing	.7	1.7	1.0	2.2
Semi-proven:				
Dry	1.4	2.8	4.3	2.9
Producing	2.7	5.2	3.1	2.7
Proven:				
Dry	0	0	0	1.3
Producing	1.5	1.3	8.0	3.0
Grand Total	9.9	13.0	23.4	20.3

The total direct costs to the Company during 1965, 1966, 1967 and 1968 of its interest in the total net wells referred to above, including lease acquisition expense and the Company's share of drilling and completion expenses, were $795,229, $1,290,178, $1,845,169 and $2,092,545, respectively. A trend of increasing cost per net exploratory well is largely attributable to the Company's increasing concentration in the testing of potentially high reserve prospects involving significant lease acquisition expense and relatively deep, remote and, therefore, expensive wells.

The eight producing net wells drilled on proven properties in 1967 reflect drilling activity by the Company in the Hoosier Field in Saskatchewan. Of the three producing net wells drilled on proven properties in 1968, 0.5 wells reflect drilling activity in the Hoosier Field, 0.4 wells reflect drilling elsewhere in Saskatchewan, and the balance reflects drilling in the United States. During fiscal 1968 the Company drilled eleven gross development wells in the Hoosier Field, seven of which were producing and four were dry.

Undeveloped Acreage

In addition to drilling prospects acquired and developed by it, since July, 1966, the Company has on occasion sold its entire interest in a prospect to others, generally major oil companies. The consideration for such sales is usually cash, although in several cases the Company retained an overriding royalty interest. Total cash received from lease sales of this type amounted to $341,026 through April 30, 1968.

At April 30, 1968, the Company's oil and gas leases, permits and concessions not held by production covered approximately 3,807,000 acres. Such properties represented an investment of approximately $2,871,000 at such date. During fiscal 1965, 1966, 1967 and 1968 the Company

expended approximately $623,000, $1,125,000, $1,828,000 and $2,323,000, respectively, for nonproducing properties. Certain information with respect to nonproducing properties owned at April 30, 1968, is set forth below:

Location	Gross Acres	Net Acres
Alberta*	347,274	201,485
British Columbia*	180,318	47,319
Manitoba*	842,949	70,392
Northwest Territories*	1,021,483	1,021,483
Ontario	43,211	4,321
Saskatchewan*	235,672	209,448
Alaska	20,413	15,309
California	11,520	101
Colorado	10,117	10,117
Kansas	3,913	3,273
Montana	173,970	116,766
Oklahoma	25,293	17,562
Texas	1,971	1,971
Wyoming	10,311	9,249
Republic of Austria	879,000	879,000
Total	3,807,415	2,607,796

* Includes drilling reservations, petroleum and natural gas reservations, permits and leases.

Offshore Activities

In July, 1967 the Company acquired 15,309 net acres of oil and gas leases in the Cook Inlet auctioned by the State of Alaska. The total purchase price of such interest was $390,498. The leases are subject to a 12½% royalty in favor of the State of Alaska and a 2½% override. The Company has conducted extensive geophysical and geological exploration on such leases representing a total expenditure at June 1, 1968 of approximately $77,000.

The Company owns 101 net acres of oil and gas leases on tracts 375 and 384 of the Santa Barbara Channel auctioned by the U. S. Government in February, 1968. The total purchase price of such interest was $660,756. The leases are subject to a 16⅔% royalty in favor of the U. S. Government. Three exploratory wells have been drilled in tract 375. An additional exploratory well is being drilled on the same tract and drilling of the first exploratory well on tract 384 has been commenced. Total exploration expenses incurred by the Company to June 1, 1968 were $4,718.

In May, 1968 the Company acquired a 7½% interest in a 5,760 acre tract offshore Texas for approximately $70,000. The lease is subject to a 16⅔% royalty in favor of the U. S. Government.

Austrian Concessions

In 1967 the Company acquired 879,000 acres of oil and gas concessions in the Republic of Austria which granted the Company the exclusive right, subject to certain conditions, to explore for oil, gas and other bituminous matter for a period of three years, which period may be extended for up to fifteen additional years. The Company has agreed to pay to the Republic of Austria customary delay rentals, field rents and royalties, including overriding royalties, amounting to not more than 10% of total production. Field studies and geophysical prospecting will be conducted by the Company in Austria before any exploratory tests are undertaken. A work program for the current year has been filed with and approved by the Republic of Austria. The Austrian concessions did not represent a significant investment by the Company at April 30, 1968.

Drilling Arrangements

During the four-year period ended April 30, 1968, the Company conducted joint drilling operations with drilling funds, 17 oil companies and six individuals. Several of such individuals are connected with the management of the Company (see "Transactions of the Company with Certain Persons"). No oil company or individual accounted for more than 11% of the Company's gross drilling arrangement expenditures during such period. However, one or more drilling funds administered or managed by Prudential Funds, Inc., or its business predecessor, Prudential Oil Corporation (herein jointly referred to as "Prudential"), have been participants in most of the Company's drilling projects during such period. Commencing in 1960, Prudential has managed a series of 16 annual or year-end drilling funds or programs (the "Funds") for oil and gas exploration and development. Participations in the Funds are offered to individual co-owners, each of whom becomes obligated to pay his proportionate amount of the costs incurred for leasehold costs, drilling and operating expenses and similar items. Prudential, as manager of the Funds, uses the facilities of a number of oil operators, including the Company, in connection with the acquisition and evaluation of drilling prospects and the drilling and completion of wells thereon. During the fiscal years 1965, 1966, 1967 and 1968 gross expenditures by the Funds in turnkey drilling arrangements conducted by the Company and for interests in leases purchased from the Company were $620,155, $903,030, $2,720,831 and $3,410,745, respectively, constituting approximately 55%, 39%, 71% and 76%, respectively, of the Company's gross revenues derived from such activities. Such amounts approximated 41%, 32%, 34% and 23%, respectively, of the Funds' total estimated drilling expenditures during the same four-year period. Since 1965, the Funds have participated in approximately 83% of the gross wells drilled by the Company, acquiring interests therein averaging 52% of the total working interest.

While the Company or its predecessors have conducted drilling arrangements with the Funds since 1960, the Company has no contracts of a continuing nature with Prudential or any of the Funds. The Funds compete with other drilling programs for moneys to expend in oil and gas ventures, and the Company competes with other operators for expenditures to be made by the Funds. There can be no assurance, therefore, that the Funds will continue to participate in the Company's drilling arrangements or that such participation will continue at its present levels.

Other Business Interests

Gilsonite Operations

Through its Mesa Chemical Co. division the Company is engaged in the business of mining, milling and marketing a solid hydrocarbon known as gilsonite. Gilsonite is a black, pitch-like substance which occurs in pure form in long, thin, nearly vertical veins in the Uinta Basin of northeastern Utah. Chemically, gilsonite approximates the composition of an asphalt-based petroleum with most of the volatile constituents absent. The Company's customers use gilsonite primarily as an additive to oil and gas drilling fluids and cements, and for ingot mold coatings. Certain grades of gilsonite are dissolved in other substances and used as a base for inks, paints and varnishes.

As of April 30, 1968, the Company's probable extractable gilsonite reserves were estimated by the Company to be approximately 469,000 tons. During the year ended April 30, 1968, the Company sold an average of approximately 553 tons of gilsonite per month. There have been no material changes in mining conditions or deposits during the past year and no such changes are presently anticipated.

CATV and Real Estate

In March, 1966, the Company acquired operating community antenna television systems serving three small Texas towns with a total population of about 11,000. The Company has franchises to serve two other communities in the area and receives microwave service from a common carrier to provide additional television channels for its subscribers. The Company also holds a franchise to construct a CATV system in Texarkana, a community of approximately 50,000 persons. However, because of the jurisdiction over CATV operations of the Federal Communications Commission, it is not known whether a CATV system in such community will be constructed. See "Competition and Regulation". At April 30, 1968, the Company's investment in operating CATV franchises aggregated approximately $158,666. An additional $7,150 is invested in the Texarkana franchise. Failure to construct facilities under the three franchises not presently in operation will not affect the Company's present investment in CATV operations, other than the probable loss of $7,150 invested in the Texarkana franchise.

The Company owns a 50% limited partnership interest in a partnership which holds an option to purchase over a 10-year period ending in 1974 approximately 2,560 acres of undeveloped real estate located about four miles north of the City of Amarillo, Texas. The Company's investment in this property aggregated $81,470 at April 30, 1968. The property will be held for investment or development.

The Company has formulated no definitive policy with regard to further investments in CATV or real estate but does not consider these ventures to be of material value in relation to its overall business operations.

Competition and Regulation

The oil and gas business is highly competitive both in the search for and acquisition of additional reserves and in the marketing of oil and gas. The Company's competitors in these endeavors include the major oil companies as well as independent oil and gas concerns and individual producers and operators. Strong competition is also encountered by the Company from other independent oil and gas operators in obtaining commitments for participations in the Company's drilling arrangements. The Company is a minor factor in the petroleum industry.

Substantially all of the Company's crude oil production is sold to purchasing companies in the various fields at current posted field prices and natural gas is sold under long term contracts. Of the Company's 24.2 net gas wells, approximately 0.7 such net gas wells are presently shut-in due to the absence of pipeline connections. These wells are in areas where applications for extension of existing transmission facilities are pending before regulatory agencies and are expected to be granted in 1969. However, there is no assurance that these applications will be granted. The marketing of this shut-in gas is dependent upon the granting of such applications, the construction of transmission facilities, and the execution of mutually agreeable sales or transmission contracts.

The Company experiences intense competition for gilsonite sales from the two other domestic gilsonite producers, one of which is substantially larger than the Company and enjoys a dominant position in the industry.

The Company is a "natural gas company" as defined in the Natural Gas Act and is, therefore, subject to regulation by the Federal Power Commission with respect to various aspects of its natural gas operations, including the sale of natural gas and the acquisition and disposition of certain natural gas properties. The principal impact of federal control upon the Company, however, is regulation of the price that it may receive for natural gas produced and sold for resale in interstate commerce in the United States.

Substantially all of the jurisdictions in which the Company owns producing oil and gas properties have statutory provisions regulating the production and sale of crude oil and natural gas. The regulations often require permits for the drilling of wells, but extend as well to the spacing of wells, the prevention of waste of oil and gas resources and other matters. In Texas, the Railroad Commission regulates the amount of oil and gas produced locally by assigning to each well an allowable rate of production. Certain other jurisdictions impose similar restrictions. The Company estimates that, as a result of the imposition of such allowables, its production for the year ended April 30, 1968 was reduced to approximately 89% of capacity with respect to oil and 41% of capacity with respect to natural gas. The Canadian market for natural gas produced in that country is not, as yet, fully developed. As a result, a substantial portion of such production is marketed under long-term contracts with pipeline companies for resale in the United States. The exportation of natural gas from Canada is subject to regulation by provincial authorities in the province of origin as well as by the National Energy Board of Canada. Reciprocally, the importation of natural gas into the United States is subject to the jurisdiction of the Federal Power Commission. Pursuant to the provisions of its concession agreements with the Republic of Austria, the Company's oil and gas activities in that country are subject to general supervision and reporting requirements administered by various departments of the Austrian government.

The Supreme Court of the United States has upheld the position of the Federal Communications Commission in asserting jurisdiction over the operation of community antenna television systems. The staff of the FCC has recommended that the CATV industry be subjected to restrictions concerning the construction and operation of new facilities as well as rates charged for its services. These restrictions may adversely affect the industry. The Supreme Court recently rejected a contention that CATV operations may require the payment of royalties under the national copyright laws.

Employee Relations

The Company has approximately 70 employees including ten geologists, two petroleum engineers and three landmen. None of the Company's employees are represented by labor unions. See "Remuneration" under "Management of the Company" for a description of the profit-sharing plans and trust agreements which the Company maintains for eligible employees. The Company contributes to group life insurance, medical, surgical, hospitalization and disability plans for all employees. The Company considers its relations with its employees to be satisfactory.

MANAGEMENT OF THE COMPANY

Directors and Officers

The following table sets forth certain information with respect to the directors and executive officers of the Company.

Name	Office
T. B. Pickens, Jr.*	President and Chairman of the Board of Directors
Lawton L. Clark	Vice President and Director
Frank W. Podpechan	Vice President
John F. Boros	Secretary-Treasurer
John D. Kirkland*	Director
Jess B. Latham, Jr.	Director
Wales H. Madden, Jr.*	Director
Don S. Marsalis	Director
J. G. O'Brien	Director
Howard F. Saunders	Director
E. H. Selecman	Director
Richard S. Smith	Director
Holland E. Toles	Director
Thomas R. Young	Director

* Member of Executive Committee.

Each of the executive officers of the Company has been in the employ of the Company or its predecessors for more than the past five years with the exception of Mr. Boros, who was employed by Arthur Andersen & Co. for more than two years prior to his employment by the Company in 1964 and Mr. Podpechan who was employed by Flag Oil Corporation and Pennant Oils Ltd. for five years preceding his employment by the Company in May, 1968.

Pursuant to an underwriting agreement relating to an offering of the Company's securities in August, 1967, New York Securities Co. has the right of first negotiation on underwritten public offerings of the Company during the next two years, and the Company has agreed that, at each annual meeting of stockholders through 1971, the list of nominees submitted by the Company management for election as directors will include one person designated by New York Securities Co. and one additional person mutually agreed upon between the Company and New York Securities Co. Richard S. Smith, a partner of New York Securities Co., is currently the director designated by New York Securities Co., and John D. Kirkland is the director designated by New York Securities Co. and the Company pursuant to such arrangement.

Remuneration

With the exception of T. B. Pickens, Jr., President of the Company, who received aggregate direct remuneration from the Company during fiscal 1968 of $31,333, none of the officers or directors of the Company received an aggregate direct remuneration from the Company and its subsidiaries during the fiscal year ended April 30, 1968, in excess of $30,000. The 13 officers and directors as a group received $92,217 as direct remuneration from the Company during the year ended April 30, 1968. The Company has agreed under certain conditions to purchase from

Mr. Pickens' estate up to $400,000 market value of the Common Stock of the Company owned by Mr. Pickens in the event of his death while employed by the Company. The Company owns life insurance policies on Mr. Pickens totaling $2,000,000. The Company pays the premiums on the policies ($51,923 annually) and is the owner and beneficiary of the policies.

The Company has two profit sharing plans and related trust agreements which were originally established by PEI and Altair, respectively, for the benefit of their several employees. The terms of the two plans are practically identical. Both provide that the Company shall make an annual contribution to the trusts from current or accumulated profits, the amount of which will be determined annually by the Board of Directors of the Company. Each plan stipulates, however, that the Company's annual contribution shall be substantial rather than nominal but in no event in excess of a maximum amount specified therein. Employees who have been employed by the Company continuously for a period of one year are eligible to participate under either plan, except that female employees must have been employed for a period of two years under the PEI plan. An amount equal to 5% of the earnings of each participating employee must be (i) withheld by the Company every pay period, (ii) remitted by the Company to the Trustee, and (iii) credited by the Trustee to the individual participant's account. The Company's annual contribution is allocated among all participants in the same proportion as their respective annual earnings bear to the total annual earnings of all participants. Amounts so accumulated are distributable under the trust agreements upon retirement and otherwise vest in the employee in varying amounts under certain circumstances. In the event the Company fails to make a required contribution or in the event the Company elects to terminate either trust, all amounts held under such trust immediately vest in the participating employees.

The amount set aside during the year ended April 30, 1968, and the amounts accrued to such date for the benefit of all officers and directors of the Company as a group were $11,220 and $48,242, respectively. The amount set aside during such year for T. B. Pickens, Jr. was $4,050 and the total amount accrued to his account at April 30, 1968 was $24,612.

Stock Options

In August, 1965, the Company adopted a Qualified Stock Option Plan (the "Plan") for key employees covering 34,651 shares of the Company's Common Stock at May 31, 1968. A three-member Stock Option Committee of directors is authorized to grant options at not less than 100% of the fair market value thereof on the date of grant. All options are restricted as to transferability and terminate not more than twelve months after death or three months after cessation of employment of the optionee and not more than five years after the grant thereof. No option may be granted under the Plan after July 22, 1975. Members of the Stock Option Committee, directors as such and holders of 5% or more of the Common Stock are not eligible to participate in the Plan.

At June 1, 1968 an aggregate of 15,983 shares of the Company's Common Stock was subject to outstanding options, of which options covering 3,025 shares at $8.89 per share expiring October 29, 1970, and 5,000 shares at $37 per share expiring May 1, 1973 were held by all officers and directors of the Company as a group. The exercise prices of all such options ranged from $8.89 to $37 per share. The expiration dates ranged from October 29, 1970 to May 1, 1973. See Note (8) of Notes to Consolidated Financial Statements of the Company.

PRINCIPAL STOCKHOLDERS OF THE COMPANY

Mr. T. B. Pickens, Jr. is the only stockholder of the Company who, as of May 15, 1968, owned of record, or was known by the Company to own beneficially, more than 10% of the outstanding Common Stock of the Company. As of that date, Mr. Pickens and members of his immediate family owned of record and beneficially 102,238 shares or approximately 13% of the Company's Common Stock. In addition, Mr. J. G. O'Brien, members of his immediate family, and family partnerships and corporations in which he and they together held a majority interest beneficially owned on such date an aggregate of 65,354 shares of Common Stock or approximately 8% of the shares outstanding.

As of May 15, 1968, the officers and directors of the Company as a group owned beneficially, directly or indirectly, an aggregate of 287,614 shares or approximately 36% of the outstanding Common Stock.

TRANSACTIONS OF THE COMPANY WITH CERTAIN PERSONS

On August 28, 1965, the Company delivered 16,039 shares of its Common Stock and $13,960 in cash to a limited partnership in exchange for the partnership's interest in certain oil and gas properties and rights located in the Hoosier Field of Saskatchewan. The partnership reserved an overriding royalty of 6% respecting all oil, gas and related hydrocarbons produced, saved and marketed from such properties. At that time, Mr. Madden, a director of the Company, owned 19% and Nabob Production Company owned 23% of such limited partnership. Mr. O'Brien, a director of the Company, is a partner of O'Brien Company which owns 100% of the outstanding capital stock of Nabob Production Company. For purposes of this exchange, the aggregate value of the oil and gas properties and rights so acquired by the Company was fixed by the parties at $146,520.

The limited partnership was dissolved on December 31, 1965, and its assets were thereafter divided among twelve partners. By virtue of this distribution, Mr. Madden acquired 3,377 shares of the Common Stock and 19% of the retained overriding royalty. Nabob Production Company received 4,221 shares of Common Stock and 23% of the overriding royalty.

Messrs. Madden, Latham, and Saunders have participated in certain joint drilling operations or ventures conducted by the Company during the last four fiscal years. In each case, the terms and conditions of their respective participations were identical to those of all other participants. The aggregate amounts of their respective investments in such operations or ventures during the last four years were $30,705, $51,549 and $9,697. During such years, (1) Mr. Madden has participated in the drilling of 12 wells (4 producers, all of which are presently shut-in) in which he has up to a 5% working interest and from which he has received no income; (2) Mr. Latham has participated in 4 wells (1 producer) in which he has a 5% working interest and from which he has received $5,348 income; and (3) Mr. Saunders has participated in 3 wells (1 producer) in which he has a 15% working interest and from which he has received $9,628 income. No additional wells are contemplated in the ventures in which Messrs. Latham and Saunders participated, and 3 more wells are contemplated in the venture in which Mr. Madden is participating. In connection with the Company's listing of its Common Stock on the American Stock Exchange the Company agreed not to permit its officers or directors to participate in any such arrangements with the Company in the future. This agreement, however, does not foreclose participation in those

arrangements entered into prior to May 15, 1967, pursuant to which the participants may be required to expend additional sums for exploration, development or acreage acquisition and may receive income in the form of royalty payments.

Mr. Richard S. Smith, a director of the Company, is a partner in New York Securities Co., which firm acted as one of the two representatives of the several underwriters in the Company's public offerings in August, 1967 of $4,000,000 principal amount of 5¾% Convertible Subordinated Debentures due 1982 and in September, 1968 of $6,500,000 principal amount of 5½% Convertible Subordinated Debentures due 1983, and received $34,125, and $........, respectively, in underwriting compensation in connection therewith.

Organizational Transactions

The Company was organized for the purpose of acquiring all of the outstanding capital stock of PEI and Altair and certain oil and gas property interests theretofore acquired by the owners thereof in part through participation in joint drilling operations or ventures with PEI or Altair.

On April 30, 1964, the Company offered to acquire all of the outstanding capital stock of PEI and Altair in exchange for the Company's Common Stock at the ratios of 2.89 shares and .83 shares, respectively, of the Company's Common Stock for each share of PEI and Altair capital stock. The exchange price of the Company's Common Stock was arbitrarily set at $8.26 per share. The value per share of PEI and Altair capital stock was fixed by certain stockholders and members of management of PEI and Altair at $35.00 and $10.00, respectively, based upon a consideration of the property owned by such corporations and the net book value and historical and prospective earnings of such corporations. On this basis, the Company acquired all of the outstanding capital stock of PEI and Altair in exchange for 219,236 shares of its Common Stock.

Also on April 30, 1964, the Company offered to exchange shares of its Common Stock for producing oil and gas interests theretofore acquired by the owners thereof primarily through participation in joint drilling ventures with PEI or Altair, although certain interests arising independently of such companies were also solicited. The number of shares offered for each of these interests was based upon an oil and gas reserve valuation developed by independent petroleum engineers. The exchange value of each property interest was obtained by estimating the net oil and gas reserves attributable to such interest and the cost of producing such reserves. From these figures an estimate of future net operating revenues attributable to each interest was obtained. Future net operating revenues were discounted by a present worth factor of 6% and the resulting figure was further discounted by a uniform 30%. The 30% discount was employed in an attempt to place realistic exchange values upon the oil and gas interests covered by the offering. The exchange ratio was fixed at one share of the Company's Common Stock for each $8.26 of property value remaining after the adjustments described above. On this basis, the Company issued, as of May 1, 1964, 289,025 shares of its Common Stock in exchange for oil and gas interests.

Interests of Certain Persons

In view of their interest in the organization of the Company, certain stockholders and members of management of PEI and Altair may be considered to have been founders or organizers of the Company. Such persons include Messrs. Lawton L. Clark, James L. Farrell, Lyman

Hunt, Don S. Marsalis, J. G. O'Brien, T. B. Pickens, Jr., Howard F. Saunders, P. D. Williams and R. E. Wolf (hereinafter sometimes called the "Organizers"). With the exception of Messrs. Hunt, Williams and Wolf, all of such persons are presently directors, officers or employees of the Company.

Pursuant to the Company's exchange offer the Organizers and their associates received an aggregate of 194,764 shares of the Company's Common Stock (approximately 38% of the original offering thereof) in exchange for 34,275 shares of PEI capital stock and 41,000 shares of Altair capital stock. For the purposes of this exchange offer, the value of the Organizers' shares of PEI and Altair capital stock, as well as the value of any shares then held by their associates, was fixed in the same manner hereinabove described respecting the valuation of all shares of PEI and Altair capital stock.

Certain of the Organizers acquired all or part of the capital stock of PEI and Altair exchanged by them within two years of the effective date of the exchange. The average cost to the Organizers of the shares so acquired was $8.23 and $1.94 per share of PEI and Altair, respectively.

Prior to April 30, 1964, several of the Organizers participated in various drilling programs or ventures conducted by PEI or Altair. Pursuant to such participations, such persons acquired interests in certain oil and gas properties for which shares of the Company's Common Stock were offered in accordance with the Company's exchange offer hereinabove described. In each case such persons participated in the programs or ventures on substantially the same basis as all other participants therein, and the number of shares of the Company's Common Stock offered in exchange for their respective property interests was determined in the same manner as hereinabove described respecting the valuation of oil and gas properties owned by other offerees.

As of May 1, 1964, the Organizers and their associates exchanged 60 separate oil and gas interests for 49,786 shares of the Company's Common Stock (approximately 17% of the original offering thereof). Certain of the oil and gas properties so exchanged by the Organizers for Common Stock of the Company were acquired by the respective owners thereof within two years of the effective date of the exchange. The average cost of such properties to the Organizers per share of the Company's Common Stock received by them was $1.22.

BUSINESS AND PROPERTY OF HUGOTON

The following description of the business and properties of Hugoton is taken from the Proxy Statements of Hugoton dated September 27, 1966 and February 5, 1968 as filed with the Securities and Exchange Commission (the Commission has not approved or disapproved or passed on the accuracy or adequacy of the Hugoton Proxy Statement) and Hugoton's Annual Report to Stockholders for 1967.

Organization

Hugoton was incorporated in the State of Delaware on September 22, 1948 and shortly thereafter issued to Panhandle Eastern Pipe Line Company ("Panhandle") in exchange for some cash and substantially the same oil and gas leaseholds as Hugoton owns today, 1,620,000 shares (adjusted for the two-for-one stock split made in March 1962) of Hugoton's presently outstanding Common Stock. Such shares were distributed by Panhandle to its stockholders in 1949.

Business

Hugoton is engaged in the production and gathering of natural gas from wells located in the Hugoton Field in the State of Kansas and in the sale of such gas solely for use in the State of Kansas. Hugoton also engages in the extraction and sale of natural gasoline and other liquefied products from the gas produced by it.

The following is a tabulation of Hugoton's gas sales and revenues therefrom for the years 1956-1967:

	MCF	Revenues		MCF	Revenues
1956	32,464,545	$4,959,645	1962	32,562,344	$5,322,708
1957	36,522,726	5,696,742	1963	37,425,285	6,140,777
1958	34,572,478	5,423,512	1964	38,037,382	7,109,078
1959	40,466,563	6,402,178	1965	36,151,219	7,042,395
1960	34,982,514	5,709,845	1966	38,029,829	7,432,574
1961	36,539,786	5,969,374	1967	42,278,388	8,263,888

Hugoton's largest gas customer is The Kansas Power and Light Company ("Kansas Power and Light") to which it sells gas for resale and for fuel in its power plants. Under the current sales contract, which was executed under date of December 24, 1962 and extends to December 31, 1982, the maximum annual sales volume increased, effective January 1, 1965, from 33,750,000 MCF to 40,000,000 MCF for 1965 and subsequent years, with a take or pay provision for 80% of the new volume. Beginning in 1968 the price for gas sold under this contract is 22¢ per MCF. Hugoton has the right to extract hydrocarbons from the gas over the life of the contract, provided that such extraction does not reduce the heating value of the gas below a monthly average of 950 BTU per cubic foot.

Production Properties and Gas Reserves

As of July 1, 1966, Hugoton owned oil and gas leaseholds on approximately 97,000 acres, all of which are producing, in the Grant and Stevens County portions of the Hugoton Gas Field of Kansas.

As of July 1, 1966, Hugoton had 174 net gas wells, all of which were connected and producing from the Chase and Council Grove Groups of Permian Age formations. One of the wells was also productive from the Morrowan Sands of Pennsylvania Age, but as of August 1, 1966 was producing only from the Council Grove formation. No oil or gas wells were drilled by Hugoton in the three years prior to July 1, 1966.

The terms of the above-mentioned leaseholds, in practically all instances, continue during the life of commercial production from wells located on the acreage embraced therein or from wells located on acreage unitized with such leasehold acreage. The gathering lines of Hugoton are located either under or over private property by virtue of rights-of-way or easements obtained from the persons who, at the time such rights-of-way or easements were obtained, were either the apparent owners thereof or, in most cases, were ascertained to be the last grantees of record of the fee title to the land involved.

The following tabulation shows the approximate miles of each of the various sizes of line pipe in Hugoton's gathering system at December 31, 1965:

Size of Line	Miles
3″	.4
4″	76.1
6″	34.9
8″	40.7
10″	4.8
12″	11.5
16″	.3
18″	3.2
20″	3.7
22″	12.9
24″	.5
Total	189.0

The following is quoted from the Hugoton 1967 Annual Report to Stockholders:

"At December 31, 1967, the Company estimates its recoverable gas reserves at 1,250,000,000 MCF. This includes the one-eighth (⅛th) royalty interest of 156,250,000 MCF."

The following letter presents a determination of Hugoton's natural gas and natural gas liquid reserves as of July 1, 1966. Production of this gas is prorated by the Kansas Corporation Commission, and, as of the date of such letter, at the then current rate of production, it was estimated that it would take 35 years to produce such reserves.

JAMES A. LEWIS ENGINEERING, INC.
Petroleum Reservoir Analysts
1700 FIDELITY UNION TOWER
DALLAS, TEXAS 75201

July 21, 1966

Mr. Michael A. Nicolais, President
Hugoton Production Company
30 Wall Street
New York, New York 10005

Dear Mr. Nicolais:

Pursuant to your request we have determined the natural gas and natural gas liquid reserves of Hugoton Production Company which are attributable to the working interests owned in the Hugoton and Panoma fields, Kansas. The effective date of this reserve report is July 1, 1966.

We estimate that as of July 1, 1966, the net proved natural gas and natural gas liquid reserves of Hugoton Production Company were 1,106,906 MMcf and 21,019,660 barrels, of which

899,332 MMcf and 17,077,940 barrels were considered developed and 207,570 MMcf and 3,941,720 barrels were undeveloped. These reserves are net to Hugoton Production Company after deducting royalties and overriding royalties owned by others. The following presents this information in more detail:

PROVED NATURAL GAS RESERVE SUMMARY

Field: Formation:	Hugoton Field Hugoton Group	Panoma Field Council Grove	Total
Gross Future Well Stream Production			
Developed Producing, MMcf	1,022,196	47,334	1,069,530
Undeveloped, MMcf	—	247,850	247,850
Total, MMcf	1,022,196	295,184	1,317,380
Net Future Well Stream Production			
Developed Producing, MMcf	892,667	41,417	934,084
Undeveloped, MMcf	—	215,590	215,590
Total, MMcf	892,667	257,007	1,149,674
Net Reserves — Sales Gas			
Developed Producing, MMcf	859,460	39,876	899,336
Undeveloped, MMcf	—	207,570	207,570
Total, MMcf	859,460	247,446	1,106,906

PROVED NATURAL GAS LIQUID RESERVE SUMMARY

	Allocated to The Kansas Power & Light Co. Contract	Unallocated As of 7/1/66	Total
Net Well Stream to be Processed — MMcf	535,369	614,305	1,149,674
Net Natural Gas Liquid Reserves — Barrels			
Gasoline (18 RVP)	2,995,080	3,436,660	6,431,740
Butanes	3,430,615	3,936,440	7,367,055
Propane	3,362,545	3,858,320	7,220,865
Total	9,788,240	11,231,420	21,019,660

The capital investment for wells and facilities which will be required for the proved undeveloped reserves stated above is estimated to be $4,550,000.

In computing the future net sales gas reserves, because of processing, applicable shrinkage and fuel requirements were deducted from the predicted net future well stream production. In the event the unallocated gas is not processed and therefore the net natural gas liquid reserves presented in the above summary are not recovered and sold, which could be the case in contracts providing for full well stream sales, the total net future reserves of sales gas would increase by 22,852 MMcf and the natural gas liquid reserves would decrease by 11,231,420 barrels. The following tabulation presents the net reserves of natural gas and natural gas liquids under this course of action:

PROVED NATURAL GAS AND NATURAL GAS LIQUID RESERVES IF UNALLOCATED NATURAL GAS IS SOLD WITHOUT PROCESSING

Net Natural Gas Reserves — Sales Gas	
Allocated to the Kansas Power & Light Co. Contract, MMcf	515,453
Unallocated as of 7/1/66, MMcf	614,305
Total, MMcf	1,129,758
Net Natural Gas Liquid Reserves — Barrels	
Gasoline (18 RVP)	2,995,080
Butanes	3,430,615
Propane	3,362,545
Total	9,788,240

As used herein, "net reserves" mean those natural gas and natural gas liquid reserves owned by Hugoton Production Company after deducting all royalties and overriding royalties. Natural gas reserves are stated in millions of cubic feet (MMcf) at 14.65 psia and 60 degrees F.

During this study the officers of Hugoton Production Company have been consulted freely and ready access was accorded to all records and data required to make this reserve study.

It was not considered necessary to make a field examination of the physical conditions of the properties. In our opinion the exisiting gas processing plant is recovering all natural gas liquids possible under the minimum BTU content restriction in the existing gas sales contract.

The character of ownership in the properties and the factual data as furnished by representatives of Hugoton Production Company were accepted as represented.

Respectfully submitted,

JAMES A. LEWIS ENGINEERING, INC.
KEITH D. SHEPPARD, P. E.
Vice President

Regulatory Matters

Hugoton produces natural gas solely from wells located in the State of Kansas and such gas is sold and consumed solely within the State of Kansas. Accordingly, such sales are not subject to the provisions of the Natural Gas Act.

The laws of the State of Kansas provide for the conservation of natural gas under the administration of the Corporation Commission of that state. Hugoton's production activities are subject to the jurisdiction of that Commission.

The following is quoted from the financial statements of Hugoton contained in its 1967 Annual Report to Stockholders and also set forth elsewhere in this Prospectus:

"Under a proceeding with the Federal Power Commission, the Company is seeking to obtain authorization for the abandonment of a sale of natural gas to Panhandle Eastern

Pipe Line Company. An Examiner's decision in this matter was issued on November 24, 1967 denying the application and ordering the Company to make refunds (with interest) of alleged excess charges for the years 1956-1965. Should the Examiner's decision be affirmed by the Commission, it is estimated that the maximum amount of the refund that would be required (with interest), net of taxes, will approximate $1,100,000.

"The Company disputes the legality of the Examiner's decision but has recently filed a settlement proposal with the Commission. This proposal would accept the denial of the abandonment and would provide for a refund of approximately $250,000 (with interest), net of taxes, which amount has been charged to retained earnings in the accompanying financial statements. If the settlement proposal is rejected by the Commission, the Company will have the opportunity to appeal the Examiner's decision."

Principal Holders of Hugoton Common Stock

The following is quoted from Hugoton's proxy statement, dated February 5, 1968, used in connection with its 1968 Annual Meeting of Stockholders:

"As of January 26, 1968, J. C. Orr & Co., nominee of Chemical Bank New York Trust Company, owned of record 210,597 shares of the Company's Common Stock constituting approximately 12.3% of the outstanding shares thereof."

DESCRIPTION OF CAPITAL STOCK OF THE COMPANY

At the Effective Date of the Exchange Offer, the total number of shares of all classes of stock which the Company shall have authority to issue will be 10,000,000, consisting of (a) 5,000,000 shares of Preferred Stock, par value $1 per share, and (b) 5,000,000 shares of Common Stock, par value $1 per share. In a Certificate of Designation, the Company will designate as the initial series of Preferred Stock the $2.50 Cumulative Convertible Preferred Stock (called the "Convertible Preferred Stock" under this heading), which will be issued in the Exchange Offer.

In the event all the outstanding Hugoton Stock is exchanged in the Exchange Offer, a total of 1,711,760 shares of Convertible Preferred Stock will be issued. The remaining authorized shares of Preferred Stock may be issued from time to time, in series, with such designations, powers, preferences, rights, qualifications, limitations and restrictions as the Board of Directors of the Company may from time to time determine.

The following is a summary of certain of the rights and provisions in respect of the Convertible Preferred Stock and Common Stock of the Company as it will exist upon consummation of the Exchange Offer, together with statements of the present rights and provisions in respect of the Preferred Stock and Common Stock. Reference is made to the Company's Certificate of Incorporation, as amended, and the Certificate of Designation, filed as exhibits to this Registration Statement, for a complete statement of the terms and provisions of the respective classes of stock, this summary being qualified in its entirety by such reference.

Dividend Rights

The holders of the Convertible Preferred Stock will be entitled to receive, prior to the payment of dividends on the Common Stock, cumulative cash dividends at the annual rate of $2.50 per share, when, as and if declared by the Board of Directors of the Company and out of the assets which are by law available for the payment of dividends, payable quarterly on the first

days of January, April, July and October in each year. After provision for payment of full cumulative dividends on the outstanding Convertible Preferred Stock, such lawful dividends may be paid on the Common Stock as the Board of Directors may deem advisable. Under the Indenture relating to the Company's 5½% Convertible Subordinated Debentures due 1983, the Company may pay dividends on any class of stock only to the extent of the Company's earnings subsequent to April 30, 1968, plus the cash proceeds of sales of capital stock subsequent to such date. Dividends will accrue from the Effective Date of Exchange or January 1, 1969, whichever is earlier.

Voting Rights

Each holder of the Convertible Preferred Stock will be entitled to one vote for each share held. Each holder of Common Stock will be entitled to one vote for each share held. Except as set forth below, the Convertible Preferred Stock and the Common Stock will vote together as one class.

Special Voting Rights

In addition to the voting rights of the holders of the Convertible Preferred Stock just referred to, such holders will have the special voting rights described below.

If the equivalent of six quarterly dividends payable on the Convertible Preferred Stock are in default, the number of directors of the Company will be increased by two, and the holders of the Convertible Preferred Stock voting as a class will be entitled to elect two directors until all dividends in default have been paid or declared and set apart for payment.

The affirmative vote or consent of the holders of at least two-thirds of the outstanding shares of the Convertible Preferred Stock will be necessary to change or abolish the relative rights, preferences or limitations of the Convertible Preferred Stock, or to authorize, or increase the authorized amount of, any class or series of stock ranking prior to the Convertible Preferred Stock as to dividends or assets.

The vote or consent of the holders of at least a majority of the outstanding shares of the Convertible Preferred Stock will be necessary to increase the authorized amount of the Preferred Stock specified in the Company's Certificate of Incorporation or to authorize, or increase the authorized amount of, any class or series of stock ranking on a parity with the Convertible Preferred Stock as to dividends or assets other than any series of Preferred Stock issued pursuant to the present authorization contained in the Certificate of Designation.

Except as otherwise required by law, no such vote or consent of the holders of at least two-thirds, or of at least a majority, as the case may be, of the outstanding shares of the Convertible Preferred Stock will be required for any merger or consolidation in which

(a) the Company is the surviving corporation, no change is made in the rights, preferences or limitations of the Convertible Preferred Stock, and no authorization is granted for any class or series of stock, or any increase in the authorized amount of any class or series of stock, if any such consent or vote would have been required for such authorization or increase immediately prior to such merger or consolidation, or

(b) the Company is not the surviving corporation, the corporation that survives shall issue in exchange for each share of Convertible Preferred Stock a share of its preferred stock with the same rights, preferences and limitations as the Convertible Preferred Stock, and

the authorized capital stock of the corporation that survives shall include only classes or series of stock for which no such consent or vote would have been required if such class or series had been authorized by the Company immediately prior to such merger or consolidation or which have the same rights, preferences and limitations and authorized amount as a class or series of stock of the Company authorized (with such consent or vote) prior to such merger or consolidation and continuing as an authorized class or series at the time thereof.

Non-Cumulative Voting

The Company's Convertible Preferred Stock and Common Stock will have non-cumulative voting rights, which means that the holders of more than 50% of the shares voting for the election of directors can elect 100% of the directors if they choose to do so, and, in such event, the holders of the remaining less-than-50% of the shares voting for the election of directors will not be able to elect any directors, except for the special voting rights of the holders of Convertible Preferred Stock in the event of certain defaults in the payment of dividends described above.

Liquidation Rights

Upon any liquidation, dissolution or winding up of the Company, the holders of the Convertible Preferred Stock will be entitled to receive $75 per share, plus all accrued and unpaid dividends, before any distribution shall be made on the Common Stock. Upon any liquidation, dissolution or winding up of the Company, the holders of Common Stock will be entitled to share ratably in assets available for distribution after provision has been made for the Convertible Preferred Stock.

Redemption and Purchase Provisions

The Convertible Preferred Stock may be called for redemption, in whole or in part, at the option of the Company on 30 days' notice at a redemption price equal to $85 per share until March 1, 1974 and $75 per share thereafter, plus dividends accrued thereon to the date fixed for redemption.

Notwithstanding these redemption provisions, if any quarterly dividend due on the Convertible Preferred Stock shall be in default, and until all such defaults shall have been cured, the Company shall not redeem any shares of Convertible Preferred Stock unless all outstanding shares of Convertible Preferred Stock are simultaneously redeemed and shall not purchase or otherwise acquire any shares of Convertible Preferred Stock except in accordance with a purchase offer made by the Company on the same terms to all holders of record of Convertible Preferred Stock. Nor shall any shares of any class of stock or series thereof ranking junior to the Convertible Preferred Stock for payment of dividends be redeemed or purchased by the Company or any subsidiary thereof (nor shall any moneys be paid to or made available for a sinking fund for the redemption of any shares of any such class or series of stock), unless in each instance dividends on all outstanding shares of Convertible Preferred Stock for all past dividend periods shall have been paid and the dividends on all outstanding shares of Convertible Preferred Stock for the then current quarterly dividend period shall have been paid or declared and sufficient funds set aside for the payment thereof.

Conversion Rights

Each share of the Convertible Preferred Stock will be convertible into Common Stock of the Company at the rate of 1.8 shares of Common Stock for each share of Convertible Preferred Stock until March 1, 1974 and at the rate of 1.6 shares of Common Stock for each share of Convertible Preferred Stock thereafter, subject to adjustment from time to time upon the occurrence of specified events. However, no adjustment will be made upon conversion in respect of any accrued but unpaid dividends. No fractional shares will be issued upon conversion, but any fractions will be adjusted in cash.

Preemptive Rights and Liability to Assessment

Holders of the Convertible Preferred Stock and the Common Stock will not be entitled to preemptive rights. The shares of Convertible Preferred Stock, when issued pursuant to the Exchange Offer, and the shares of Common Stock issuable upon conversion of the Convertible Preferred Stock, when issued upon conversion thereof, will be fully paid and non-assessable.

Transfer Agents and Registrars

The Transfer Agent and Registrar for the Convertible Preferred Stock is the Irving Trust Company, New York, New York. The Transfer Agents and Registrars for the Common Stock are The First National Bank of Amarillo, Amarillo, Texas, and The Chase Manhattan Bank (National Association), New York, New York.

DESCRIPTION OF CAPITAL STOCK OF HUGOTON

Hugoton has authorized 4,000,000 shares of common stock, par value $1.00 per share, of which 1,711,760 shares were issued and outstanding at December 31, 1967. Each share entitled the holder thereof to one vote on all matters submitted to the stockholders. In the event of liquidation or dissolution, the holders of the common stock will share ratably in the net assets of Hugoton. The common stock is not subject to redemption and has no conversion rights. The preemptive rights of stockholders have been denied. The holders of the common stock are entitled to such dividends as may be declared by the Board of Directors of Hugoton from time to time out of funds legally available therefor. The Hugoton shares do not have cumulative voting rights.

DEALER MANAGERS

The Dealer Managers, for whom New York Securities Co. and Bacon, Whipple & Co. are acting as Representatives, and their shares are as follows:

Dealer Manager	Address	Manager's Share
New York Securities Co.	One Whitehall Street, New York, New York 10004	%
Bacon, Whipple & Co.	135 South La Salle Street, Chicago, Illinois 60603	

Dealer Manager	Address	Manager's Share
	Total	100%

For a description of the soliciting dealer arrangements, see "The Exchange Offer — Solicitation of Acceptances" herein.

LEGAL OPINIONS

Legal matters in connection with this offering are being passed upon for the Company by Messrs. Baker, Botts, Shepherd & Coates, 1600 Esperson Building, Houston, Texas 77002, and for the Dealer Managers by Messrs. White & Case, 14 Wall Street, New York, New York 10005.

EXPERTS

The financial statements and schedules for the four years ended April 30, 1968, with respect to the Company, included in this Prospectus and elsewhere in the Registration Statement have been examined by Arthur Andersen & Co., independent public accountants, as indicated in their reports with respect thereto, and are included herein in reliance upon the authority of said firm as experts in giving said reports.

The report of Messrs. DeGolyer and MacNaughton set forth in this Prospectus beneath the subcaption "Reserves" under the caption "Business and Property of the Company" has been included herein on their authority as experts respecting the matters contained therein.

ADDITIONAL INFORMATION

The Company has filed with the Securities and Exchange Commission, Washington, D. C., a Registration Statement under the Securities Act of 1933, as amended, with respect to the securities offered hereby. For further information with respect to the Company and the securities offered by this Prospectus, reference is made to the Registration Statement and the financial statements and exhibits filed as a part thereof. Statements contained in this Prospectus as to the contents of any contract or other document are not necessarily complete, and in each instance reference is hereby made to the copy of such contract or other document filed as an exhibit to the Registration Statement for a full statement of the provisions thereof, and each such statement in this Prospectus is qualified in all respects by such reference.

INDEX TO FINANCIAL STATEMENTS

SOURCE OF FINANCIAL STATEMENTS OF HUGOTON

The balance sheet, statements of income, statements of paid-in capital and retained earnings, and the related notes to the financial statements of Hugoton Production Company, which are included in the Registration Statement and in this Prospectus have been taken from Hugoton's (1) 1967 annual report to stockholders, (2) proxy statement for the special meeting of stockholders to be held on October 27, 1966, filed with the Securities and Exchange Commission, (3) 1965, 1966, and 1967 annual reports on Form 10-K, filed with the Securities and Exchange Commission and (4) quarterly statement as of June 30, 1968. In this regard, it should be noted that the Securities and Exchange Commission does not approve or disapprove, or pass upon the accuracy or adequacy of the statements and reports filed with it.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Mesa Petroleum Co.

We have examined the consolidated balance sheet of Mesa Petroleum Co. (a Delaware corporation) and subsidiaries as of April 30, 1968, and the related consolidated statements of reinvested earnings, and capital surplus for the three years then ended. We have also examined the consolidated statements of income for the four years ended April 30, 1968. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements set forth above present fairly the financial position of Mesa Petroleum Co. and subsidiaries as of April 30, 1968, and the results of their operations for the four years then ended, in conformity with generally accepted accounting principles consistently applied during the periods, after giving retroactive effect to the change in accounting for the ten per cent stock distribution in March, 1967 as set forth in the accompanying consolidated statements of reinvested earnings and capital surplus.

ARTHUR ANDERSEN & CO.

Houston, Texas
June 5, 1968

MESA PETROLEUM CO. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET
April 30 and July 31, 1968

ASSETS	April 30, 1968	July 31, 1968 (Unaudited)
Current Assets:		
Cash	$ 552,818	$ 666,769
Accounts receivable:		
Oil and gas operations	2,235,801	1,564,399
Other	67,691	94,430
Inventories, at cost (Note 9):		
Oil and gas leases held for resale within one year	1,234,924	1,376,289
Gilsonite products	37,548	39,045
Prepaid expenses	33,453	38,370
Total current assets	$ 4,162,235	$ 3,779,302
Investments, at cost:		
Canadian government bonds	$ 38,765	$ 38,765
Real estate partnership	81,470	81,470
Marketable securities (market value $406,040 and $977,325)	452,106	775,886
	$ 572,341	$ 896,121
Property, Plant, and Equipment, at cost, substantially pledged to secure long-term debt (Notes 2, 3 and 4):		
Producing and nonproducing oil and gas leases, wells and equipment	$ 9,694,092	$10,210,122
Gilsonite mining properties, plant, and equipment	1,155,870	1,158,299
Automotive, office and other properties	357,936	371,402
	$11,207,898	$11,739,823
Less — Accumulated depreciation, depletion and amortization	1,591,926	1,742,006
	$ 9,615,972	$ 9,997,817
Deferred Charges and Other Assets:		
Cash surrender value of life insurance	$ 105,483	$ 111,483
Deferred charges	69,982	90,505
	$ 175,465	$ 201,988
	$14,526,013	$14,875,228
LIABILITIES		
Current Liabilities:		
Current maturities on long-term debt	$ 11,500	$ 11,000
Accounts payable and accrued liabilities	804,598	839,919
Royalties payable	121,163	104,558
Total current liabilities	$ 937,261	$ 955,477
Long-Term Debt, net of current maturities (Note 6)	$ 3,880,465	$ 3,878,573
Deferred Income from Sale of Production Payment (Note 5)	$ 220,105	$ 178,802
Deferred Federal Income Taxes	$ —	$ 69,958
Stockholders' Investment (Notes 2, 3, 7 and 8):		
Preferred stock, $1 par value; authorized 1,000,000 shares; none issued		
Common stock, $1 par value; authorized 5,000,000 shares; issued and outstanding 798,659 shares	$ 798,659	$ 798,659
Capital surplus	7,835,556	7,835,556
Reinvested earnings	853,967	1,158,203
	$ 9,488,182	$ 9,792,418
	$14,526,013	$14,875,228

(See accompanying notes to financial statements.)

MESA PETROLEUM CO. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF REINVESTED EARNINGS

	Year Ended April 30			Three Months Ended July 31, 1968 (Unaudited)
	1966	1967	1968	
Balance, beginning of period, as previously reported	$ 414,308	$1,073,200	$2,027,670	$ 853,967
Net income for the period	706,560	1,007,670	1,389,755	344,166
Dividends paid — Cash	(47,668)	(53,200)	(58,574)	(39,930)
Stock	—	—	(1,755,310)	—
Balance, end of period, as previously reported	$1,073,200	$2,027,670	$1,603,541	$1,158,203
Adjustment to transfer to capital surplus the market value of 53,199 shares of common stock issued in a 10% stock dividend paid in March, 1967 which had previously been accounted for as a stock split	—	(749,574)	(749,574)	—
Balance, end of period, as adjusted	$1,073,200	$1,278,096	$ 853,967	$1,158,203

CONSOLIDATED STATEMENTS OF CAPITAL SURPLUS

	Year Ended April 30			Three Months Ended July 31, 1968 (Unaudited)
	1966	1967	1968	
Balance, beginning of period, as previously reported	$1,368,009	$1,837,314	$1,784,115	$7,835,556
Excess of recorded costs over par value of 121,000 shares of common stock issued as consideration for the acquisition of the net assets of Standard Gilsonite Company (Note 3)	350,000			
Excess of recorded costs over par value of 16,039 shares of common stock issued as partial consideration for the acquisition of certain oil and gas property interests (Note 3)	119,305			
Transfer to capital stock on stock split, effected in the form of a stock dividend (see adjustment below)		(53,199)		
Excess market value over par value of 10% stock dividend			1,696,308	
Excess of conversion amount over par value of 152,817 shares of common stock issued in connection with the conversion of $3,979,000 of 5¾% Convertible Subordinated Debentures due 1982, less unamortized bond issuance costs of $215,779 (Note 7)			3,610,404	
Excess cost over proceeds received from sale of treasury stock to officers and key employees under stock option plan			(4,845)	
Balance, end of period, as previously reported	$1,837,314	$1,784,115	$7,085,982	
Adjustment to transfer from reinvested earnings to capital surplus the market value of 53,199 shares of common stock issued in a 10% stock dividend paid in March, 1967 which had previously been accounted for as a stock split		749,574	749,574	
Balance, end of period, as adjusted	$1,837,314	$2,533,689	$7,835,556	$7,835,556

(See accompanying notes to financial statements.)

MESA PETROLEUM CO. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Principles of Consolidation:

The consolidated financial statements include the accounts of the parent, Mesa Petroleum Co., and its five totally held subsidiaries. All significant intercompany transactions have been eliminated. Conversion from foreign currency, where necessary, was made in accordance with generally accepted accounting principles and differences resulting from exchange fluctuations are insignificant.

(2) Organization:

Mesa Petroleum Co. was organized in February, 1964, and began operations on May 1, 1964, when it acquired in a tax-free exchange (a) all of the outstanding shares of capital stock of Petroleum Exploration, Inc. of Texas and Altair Oil & Gas Co. in exchange for 219,236 shares of common stock, and (b) certain interests in oil and gas properties in exchange for 289,025 shares of common stock. The capital stock of the two companies acquired has been recorded in the accounts of Mesa at the aggregate underlying book value of these companies, $571,000, as of date of acquisition. Both Altair Oil & Gas Co. and Petroleum Exploration, Inc. of Texas were merged into Mesa as of April 30, 1967. The interests in the oil and gas properties acquired were recorded at $1,282,382 which represented depreciated historical cost reduced by the unavailable Federal income tax benefits applicable to the difference between such recorded costs and the tax basis of the properties acquired in the tax-free exchange. The excess, $1,433,330, of the recorded costs of the above acquisitions over the par value of the common stock issued therefor was credited to capital surplus, net of stock issuance expense of $65,321.

(3) Acquisition of Standard Gilsonite Company and Oil Properties:

In September, 1965, the Company acquired substantially all of the assets and assumed the stated liabilities of Standard Gilsonite Company in exchange for 121,000 shares of common stock. The shares issued in connection with this acquisition were recorded at values as determined by the board of directors. The values thus determined totaled $450,000, which represented the book value of the 121,000 shares of Mesa stock as of the date of acquisition, reduced by the unavailable Federal income tax benefits applicable to the difference between such recorded value and the tax basis of the assets acquired in the tax-free exchange. This value together with the liabilities assumed also closely approximated the historical cost of the properties of the predecessor company had that company followed the policy of capitalizing all mine development costs and preoperating expenses. Of the total recorded value of the shares issued $100,000 was credited to capital stock with the balance ($350,000) credited to capital surplus.

In November, 1965, the Company issued 16,039 shares of stock as partial consideration for interests in certain oil and gas properties. The shares issued were recorded in an amount equal to the fair market value of the interests acquired as determined by the board of directors which was based on cash offerings for such interests. The fair market value of the interests acquired in exchange for the stock issued was $132,560, of which $13,256 was credited to capital stock with the balance ($119,305) credited to capital surplus.

(4) Accounting Policy Relating to Oil and Gas Properties, Depreciation, and Maintenance:

The Company follows the accounting policy of capitalizing, for financial reporting purposes, all direct costs incurred in the acquisition, exploration, and development of gas and oil

reserves, including nonproductive costs. Such capitalized costs are being amortized on a company-wide composite unit-of-production method over the aggregate productive life of all of its producing properties. Under this method of accounting, no gains or losses are recognized upon the sale or disposition of oil and gas properties, except in extraordinary transactions. Through July 31, 1968, nonproductive costs capitalized, net of gains on sales of producing properties which have been credited to property, amounted to approximately $1,675,000.

Gilsonite properties, other than mine and mill equipment, are amortized on the unit-of-production method. Depreciation of mine and mill equipment and other equipment is provided on the straight-line method of depreciation at the following rates:

Type of Property	Rate
Office furniture and fixtures	10%
Automotive equipment	20–33⅓%
Buildings, machinery and equipment	10–12½%

It is the practice of the Company to charge maintenance and repairs against income when incurred. Renewals and betterments which extend the useful life of the equipment are capitalized.

(5) Sale of Production Payment:

In April, 1966, the Company sold interests in future production (production payment) from certain of its oil and gas properties for $550,000. The principal amount, plus an amount equivalent to interest of 6¾ percent on the unpaid balance, is payable out of 80 percent of the company's share in production from the properties. The proceeds from the sale have been deferred for financial reporting purposes and are being taken into income as the oil and gas are produced.

(6) Long-Term Debt:

On March 15, 1968, the Company entered into a revolving credit agreement with a bank under which it may borrow up to $3,860,000 at any time before May 15, 1969, at an interest rate of 6¾ percent. The bank has also agreed to make a term loan to the Company at May 15, 1969 in an amount not to exceed $3,860,000. The loan would be repayable in sixty-six monthly installments and bear interest at ¾ of 1 percent above the then prime rate or 6¾ percent, whichever is greater. The loan agreement contains certain provisions and restrictions pertaining to dividend payments, working capital, net worth, capital expenditures and other matters. The loan was completely liquidated on September 13, 1968, and the bank's obligation to make further credit advances and the term loan to the Company at May 15, 1969 will be renegotiated.

Long-term debt and other obligations at July 31, 1968, consisted of the following:

	Long-term	Current	Total
6¾% revolving credit note payable to a bank secured by mortgages on substantially all producing oil and gas properties	$3,860,000	$ —	$ 3,860,000
Noninterest-bearing purchase obligation, payable at the rate of $2 per ton of ore removed from certain gilsonite properties	18,073	11,000	29,073
Other	500	—	500
	$3,878,573	$11,000	$3,889,573

The following tabulation sets forth, for the next five fiscal years, the minimum amounts payable on the long-term debt as of July 31, 1968:

1969	$ 11,000	1972	$701,819
1970	713,319	1973	701,819
1971	710,784		

(7) Capital Stock and Sale of Convertible Debentures:

In September, 1967, the stockholders approved an increase from 1,000,000 to 5,000,000 in the number of authorized shares of common stock. At the same time, the stockholders also authorized a new class of preferred stock consisting of 1,000,000 shares with a par value of $1. Through April 30, 1968, no preferred shares had been issued.

On August 2, 1967, the Company sold $4,000,000 principal amount of Convertible Subordinated Debentures due 1982. The Debentures were convertible at the option of the holder into common stock of the Company at the rate of $25.91 principal amount of debentures per share.

On January 12, 1968, the Company called for redemption the Convertible Debentures and the holders thereof exercised their option and exchanged $3,979,000 principal amount of Debentures for 152,817 shares of common stock. The remaining $21,000 of Debentures were redeemed by the Company.

On September 13, 1968, the Company sold $6,500,000 principal amount of Convertible Subordinated Debentures due 1983. The Debentures are convertible at the option of the holder into common stock of the Company at the rate of $45 principal amount of debenture per share. Proceeds from the sale were used to liquidate the Company's bank loan and the remainder was added to working capital. The indenture relating to these debentures contains certain provisions among which (1) the Company may pay dividends on any class of stock only to the extent of the Company's earnings subsequent to April 30, 1968, plus the cash proceeds of sales of capital stock subsequent to such date, and (2) under certain conditions, the Company is prohibited from incurring any senior funded indebtedness.

(8) Stock Options:

Under a qualified stock option plan approved by the stockholders in 1965, 34,651 shares of authorized and unissued common stock are reserved for options which may be granted to officers and key employees at prices equivalent to market value on the date of grant. The options become exercisable in four annual installments commencing one year after the date granted and if not exercised, expire five years after the date of grant. Upon exercising of options the Company credits the capital stock account with the par value of the shares purchased and credits the balance of the cash received to capital surplus and no charge is made to income.

Information for the three years ended April 30, 1968 and for the three month period ended July 31, 1968 with respect to options granted, after giving effect to stock dividends, is set forth below:

	Number of Shares	Option Price		Market Value, at Date Granted, When Exercisable or Exercised	
		Per Share	Total	Per Share	Total
Shares under Option at July 31, 1968, and granted during the fiscal year —					
1966	7,260	$8.89	$ 64,541	$8.89	$ 64,541
1967	1,623	$12.40-$19.09	22,885	$12.40-$19.09	22,885
1968	2,100	$22.73-$36.63	61,625	$22.73-$36.63	61,625
1969	5,000	$37.00	185,000	$37.00	185,000
	15,983		$334,051		$334,051
Options which became exercisable during the fiscal year —					
1967	2,571	$8.89	$ 22,856	$11.12	$ 28,590
1968	3,011	$8.89-$19.09	29,228	$27.16-$38.75	87,084
1969	—	—	—	—	—
	5,582		$ 52,084		$115,674
Options exercised during the fiscal year —					
1967	—	—	—	—	—
1968	1,649	$8.89-$19.09	$ 16,057	$34.25	$ 56,478
1969	—	—	—	—	—

(9) **Inventories:**

Inventories of oil and gas leases used in the computation of cost of drilling arrangements and oil and gas leases held for resale and cost of gilsonite sales are summarized as follows:

	Oil and Gas Leases Held for Resale	Gilsonite Products
May 1, 1964	$ 152,175	$ —
April 30, 1965	356,426	—
April 30, 1966	388,890	13,144
April 30, 1967	485,205	32,021
April 30, 1968	1,234,924	37,548
July 31, 1968	1,376,289	39,045

Oil and gas leases held for resale are valued at actual cost, and gilsonite products are valued at average cost which is not in excess of market.

(10) Supplementary Profit and Loss Information for the Three Years Ended April 30, 1968 and the Three Months Ended July 31, 1968 (Unaudited):

	Capitalized as Oil and Gas Properties	Charged Directly to Profit and Loss: Operating Expense	Charged Directly to Profit and Loss: Administrative and General Expenses	Total
1966				
Rentals	$ 87,878	$ —	$ 13,880	$101,758
Maintenance and repairs	$ —	$ *	$ —	$ —
Taxes —				
Production	$ —	$ 30,791	$ —	$ 30,791
Payroll	—	—	6,231	6,231
Ad valorem and other taxes	—	*	19,980	19,980
	$ —	$ 30,791	$ 26,211	$ 57,002
1967				
Rentals	$148,336	$ —	$ 26,430	$174,766
Maintenance and repairs	$ —	$ *	$ —	$ —
Taxes —				
Production	$ —	$ 38,835	$ —	$ 38,835
Payroll	—	—	18,699	18,699
Ad valorem and other taxes	—	*	17,228	17,228
	$ —	$ 38,835	$ 35,927	$ 74,762
1968				
Rentals	$265,531	$ —	$ 32,653	$298,184
Maintenance and repairs	$ —	$ *	$ —	$ —
Taxes —				
Production	$ —	$ 44,329	$ —	$ 44,329
Payroll	—	—	20,860	20,860
Ad valorem and other taxes	—	*	11,650	11,650
	$ —	$ 44,329	$ 32,510	$ 76,839
Three Months Ended July 31, 1968 (Unaudited)				
Rentals	$ 42,222	$ —	$ 10,745	$ 52,967
Maintenance and repairs	$ —	$ *	$ —	$ —
Taxes —				
Production	—	10,011	—	10,011
Payroll	—	—	6,254	6,254
Ad valorem and other taxes	—	*	4,046	4,046
	$ —	$ 10,011	$ 10,300	$ 20,311

* Information not segregated in the accounts.

Oil and gas royalties paid have been excluded from sales. No management and service contract fees have been paid during any of the periods, and maintenance and repairs were not significant.

HUGOTON PRODUCTION COMPANY

BALANCE SHEET

December 31, 1967 and June 30, 1968

ASSETS

	December 31, 1967	June 30, 1968
Current Assets:		
Cash	$ 1,487,355	$ 1,458,074
Marketable securities, at cost less amortization of premium which approximates market	2,098,906	3,300,294
Accounts receivable	952,720	635,774
Inventory and supplies, at average cost	103,948	100,595
Prepayments	6,772	23,300
Total current assets	4,649,701	5,518,037
Investment securities, at cost (Note 2)	773,855	773,855
Plant, property and equipment, at original cost (Note 3)	14,471,646	14,467,047
Less accumulated depreciation, depletion and amortization	4,720,027	4,962,124
	9,751,619	9,504,923
	$15,175,175	$15,796,815

LIABILITIES

	December 31, 1967	June 30, 1968
Current Liabilities:		
Accounts payable	$ 196,671	$ 95,789
Accrued Federal income tax (Note 1)	2,321,748	2,519,920
Other accrued liabilities	82,964	10,038
Reserve for possible refund, net (Note 4)	250,000	250,000
Total current liabilities	2,851,383	2,875,747
Stockholders' Equity:		
Common stock, $1.00 par value per share. Authorized 4,000,000 shares; issued 1,711,760 shares	1,711,760	1,711,760
Paid-in capital	318,839	318,839
Retained earnings (Note 1)	10,293,193	10,890,469
	12,323,792	12,921,068
	$15,175,175	$15,796,815

(See accompanying notes to financial statements.)

HUGOTON PRODUCTION COMPANY

STATEMENTS OF PAID-IN CAPITAL AND RETAINED EARNINGS

For the Three Years and Six Months Ended June 30, 1968

	1965	1966	1967	Six Months Ended June 30, 1968
Paid-In Capital:				
Balance, at beginning of period	$ 237,309	$ 266,447	$ 318,839	$ 318,839
Excess of proceeds over par value of common stock issued under the stock option plan (Note 6)	29,138	52,392	—	—
Balance, at end of period	$ 266,447	$ 318,839	$ 318,839	$ 318,839
Retained Earnings:				
Balance, at beginning of period	$ 9,581,536	$ 8,941,769	$ 9,340,833	$10,293,193
Provision for possible refund, net of income tax of $180,000 (Note 4)	—	—	(250,000)	—
Net income for the period	3,634,238	3,820,799	4,625,880	2,309,036
Cash dividends on common stock	(4,274,005)	(3,421,735)	(3,423,520)	(1,711,760)
Balance, at end of year	$ 8,941,769	$ 9,340,833	$10,293,193	$10,890,469

(See accompanying notes to financial statements.)

HUGOTON PRODUCTION COMPANY

NOTES TO FINANCIAL STATEMENTS

(1) On April 20, 1966, the Internal Revenue Service proposed deficiencies in Hugoton's Federal income taxes for the years 1958-1964 in the amount of $1,843,045, which, with interest (net of taxes), would approximate $2,150,000. The proposed deficiencies are based primarily on a recomputation of the depletion deduction under the method employed by the Court of Claims in its 1965 decision relating to Hugoton's Federal income tax liability for the years 1952-1957. A protest has been lodged against the proposed deficiencies and the matter is now pending before the Appellate Division of the Regional Commissioner's Office at Wichita, Kansas.

A settlement offer of $1,140,000, exclusive of interest, has been made to the Appellate Division covering all years through 1964. The offer has been recommended for acceptance by the Appellate Conferee, with the final acceptance subject to review and approval by the Appellate Division Review, at Oklahoma City, Oklahoma. As of the current date, the settlement offer is pending.

Although it is not possible to determine the ultimate liability for such years until the various issues are resolved, provision was made retroactively, during 1966, for estimated additional income taxes (plus interest, net of taxes) for the years 1958-1964 in the amount of $1,500,000. Additionally, since any settlement of the proposed deficiencies for such years may also be applicable to subsequent years, the provisions for Federal income taxes for the years 1965-1967 have been made on a basis consistent with the assumptions used in recording the estimated additional liability for prior years.

Should the position of the Internal Revenue Service ultimately prevail for the period 1958-1964 and subsequent years, an additional liability (including interest, net of taxes) estimated to approximate $800,000 would be incurred.

Hugoton has had the benefit for Federal income tax purposes of certain deductions such as intangible development costs, which have not been written off on the books. The investment tax credit (of immaterial amount) has been reflected as a reduction of the provision for Federal income taxes.

(2) Investment securities consist of the following shares of common stock:

			Market Value	
	Number of shares	Cost	December 31, 1967	June 30, 1968
Kansas Power & Light Company	15,000	$215,910	$ 300,000	$ 350,625
National Distillers and Chemical Corporation	20,000	557,945	785,000	815,000
		$773,855	$1,085,000	$1,165,625

(3) Plant, property and equipment includes $135,000 representing the amount at which oil and gas leases initially acquired were carried on the books of Panhandle Eastern Pipe Line Company, the predecessor owner. Depreciation, depletion and amortization of plant properties are provided generally on a unit of production basis.

The provision for depreciation, depletion and amortization includes depreciation on certain items (chiefly equipment, minor in amount) at per annum rates ranging from 5% to 33⅓%, and an amount for the remaining plant properties (including organization fees and expense) computed on the basis of units of gas withdrawn. At the time properties are disposed of, the original cost (or estimated original cost), less net salvage value, of property disposed of is charged to the accumulated depreciation, depletion and amortization.

Intangibles consist principally of a gas sales contract purchased during the year which is being amortized over its remaining life to June 30, 1985. Such amortization is credited direct to the asset account.

Maintenance and repairs; depreciation, depletion and amortization of plant; and taxes other than taxes on income; are shown in the statement of income and have been charged to operating expenses, except for nominal amounts of (a) depreciation charged to the transportation expense clearing account and (b) taxes charged to construction work in process and other accounts. It is not practicable to compile the amounts of maintenance and repairs which have been charged to the transportation expense clearing account and redistributed together with other charges to various operation, construction and other accounts; however, the amounts of such maintenance and repairs are not material. There were no management and service contract fees, and rents and royalties (other than gas royalties) were not significant.

The significant taxes, other than taxes on income, are set forth below:

	1965	1966	1967
Ad Valorem	$145,344	$173,213	$258,285
Other (payroll, franchise, compensating use and other)	24,844	29,966	45,405
	$170,188	$203,179	$303,690
Charged to operating expenses	$169,227	$202,319	$302,612
Charged to construction and other accounts	961	860	1,078
	$170,188	$203,179	$303,690

(4) Under a proceeding with the Federal Power Commission, Hugoton is seeking to obtain authorization for the abandonment of a sale of natural gas to Panhandle Eastern Pipe Line Company. An Examiner's decision in this matter was issued on November 24, 1967 denying the application and ordering Hugoton to make refunds (with interest) of alleged excess charges for the years 1956-1965. Should the Examiner's decision be affirmed by the Commission, it is estimated that the maximum amount of the refund that would be required (with interest), net of taxes, will approximate $1,100,000.

Hugoton disputes the legality of the Examiner's decision but has recently filed a settlement proposal with the Commission. This proposal would accept the denial of the abandonment and would provide for a refund of approximately $250,000 (with interest), net of taxes, which amount has been charged to retained earnings in the accompanying financial statements. If the settlement proposal is rejected by the Commission, Hugoton will have the opportunity to appeal the Examiner's decision.

(5) Reference is made to Note (c) to Hugoton's Statements of Income appearing elsewhere herein for a description of Hugoton's pension plan.

(6) Hugoton had a Key Employees' Restricted Stock Option Plan pursuant to which nontransferable options covering 50,000 shares of authorized but unissued common stock could be granted to not more than 12 key employees (including officers) of Hugoton at a price which was at least 95% of the fair market value on the date of the grant of the option. Under this plan Hugoton granted options covering the right to purchase up to 10,760 shares of common stock at $28.75 per share, which was approximately the market price at the date of the grant. The options were exercisable beginning one year from the date of option, with all options expiring on February 17, 1967.

Information for years 1965, 1966, and 1967 with respect to options granted is set forth below:

	Number of shares	Option price		Market value at date when exercisable or exercised	
		Per share	Total	Per share	Total
Options which became exercisable during the year —					
1965	1,076	$28.75	$30,935	$53.25	$57,297
1966	1,076	$28.75	$30,935	$47.75	$51,379
1967	—	—	—	—	—
Options exercised during the year —					
1965	1,050	$28.75	$30,188	$47.625-$53.25	$53,569
1966	1,888	$28.75	$54,280	$42.25-$58.00	$93,876
1967	—	—	—	—	—

The excess of the total consideration received over the par value of $1.00 per share has been credited to paid-in capital in accordance with Hugoton's plan of accounting for the options when exercised.

Financial Review *For The Years Ended April 30*

MESA
PETROLEUM CO.

	1968	1967
Gross revenues	$6,188,000	$5,269,000
Cash flow	$1,899,000	$1,397,000
Per share*	$ 2.71	$ 2.18
Net income	$1,390,000	$1,008,000
Per share*	$ 1.98	$ 1.56
Cash dividends paid	$ 59,000	$ 53,000
Per share	$ .09	$ .08
Stock dividend paid	10%	10%
Stockholders' equity	$9,488,000	$4,378,000
Per share*	$ 13.53	$ 6.80
Average number of shares outstanding during each period	701,335	643,710
Oil and condensate sales — net bbls.	329,000	252,000
Gas sales — net Mcf.	3,691,000	3,187,000
Wells drilled —		
Gross	74	77
Net	20.3	23.4

* Based on average number of shares outstanding during each period, after giving retroactive effect to a 10% stock split in March, 1967, and a 10% stock dividend in January, 1968.

President's Letter

On April 30, 1968, Mesa concluded its fourth year of operation since its organization in 1964. For the third straight year record highs were set in virtually all areas of Mesa's business. Gross revenues totaled $6,187,825, an increase of $919,017 over the $5,268,808 reported in fiscal year 1967. Net income was $1,389,755 compared with $1,007,670 last year, an increase of $382,085. Earnings per share increased 27% to $1.98 based on 701,335 average shares outstanding, compared to $1.56 for last year, with 643,710 average shares outstanding. Cash flow increased 36% from $1,397,117 to $1,899,110.

During fiscal 1968 Mesa distributed a 10% stock dividend, the second in the past two years, and also paid its regular cash dividend.

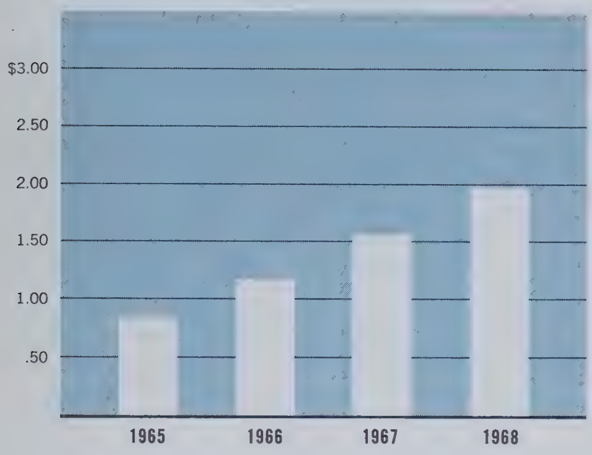
In August, 1967, the Company sold $4,000,000 principal amount of 5¾% Convertible Subordinated Debentures due 1982. The Debentures were convertible at the option of the holder into common stock of the Company at the rate of $25.91 principal amount of debentures per share. In January, 1968, the Company called the debentures for redemption. Most holders exercised their conversion option and exchanged $3,979,000 principal amount of debentures for 152,817 shares of common stock. The remaining $21,000 were redeemed for cash.

Sales of oil and gas increased approximately 22% over the last fiscal year. At year end the Company had interests in 16 (2.3 net) shut-in gas wells, a substantial number of which should be connected to pipelines within the next twelve months. On April 30, Mesa's undeveloped acreage position was the largest in its history, totaling approximately 1.7 million net acres of leases, reservations and permits in the U. S. and Canada.

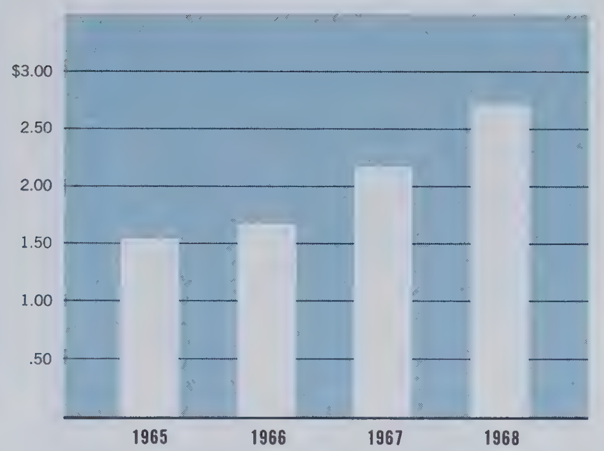
In 1967 Mesa acquired 15,309 net acres of oil and gas leases at a competitive sale in the Cook Inlet Basin of Alaska for $390,000. The Company has conducted extensive geophysical and geological studies on these leases and present plans are to drill an exploratory well in the Cook Inlet during the late summer or fall of this year.

At a Federal lease sale held in February, Mesa acquired 101 net acres of oil and gas leases in two 5,760 acre tracts (375 and 384) in the Santa Barbara Channel offshore California at a cost of approximately $660,000. Two unsuccessful exploratory wells have been drilled on Tract 375 and a third well is currently drilling. Tract 384 has not been tested; however, an exploratory well is scheduled within the next few months.

In May, 1968, Mesa along with a group of other operators bid on a number of tracts at a Federal



NET INCOME PER SHARE



CASH FLOW PER SHARE

offshore Texas lease sale. The Company acquired a 7½% interest in a 5,760 acre tract for approximately $70,000. To date no drilling has been undertaken on this acreage.

During the next fiscal year, Mesa's oil and gas exploration and development drilling program is anticipated to be the largest ever undertaken by the Company. Gross capital expenditures which includes expenditures by partners in wells in which Mesa is operator, should be about $10,000,000 of which Mesa's share is expected to be approximately $3,000,000. Major exploration activity will be in British Columbia, Alberta, the Rocky Mountain area, Anadarko Basin and the offshore areas of California, Alaska and Texas.

On June 24, 1968, Mesa filed a Registration Statement with the Securities and Exchange Commission for the proposed sale of $6.5 million of Convertible Subordinated Debentures due 1983. The offering is expected to be made early in August through an underwriting group headed by New York Securities Co. and Bacon, Whipple and Co. Part of the proceeds from the sale of the debentures will be used to retire outstanding bank indebtedness and the balance will be added to working capital.

In May, 1968, Mr. Frank W. Podpechan was named Vice President and General Manager of our Canadian operations. During the past year we were fortunate in being able to add the following to our Board of Directors: Mr. John D. Kirkland, Group Vice President — Corporate Finance for Pennzoil United, Inc., Houston; Mr. Richard S. Smith, Partner of New York Securities Co., New York, and Mr. E. H. Selecman, Partner of Selecman & Madden.

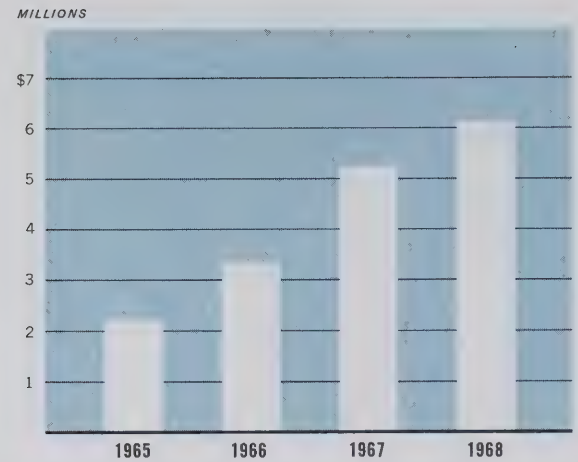
Combining our sound financial structure with a capable organization, we are confident that your Company will continue to expand its business throughout the coming year.

Sincerely,

T. B. Pickens, Jr.

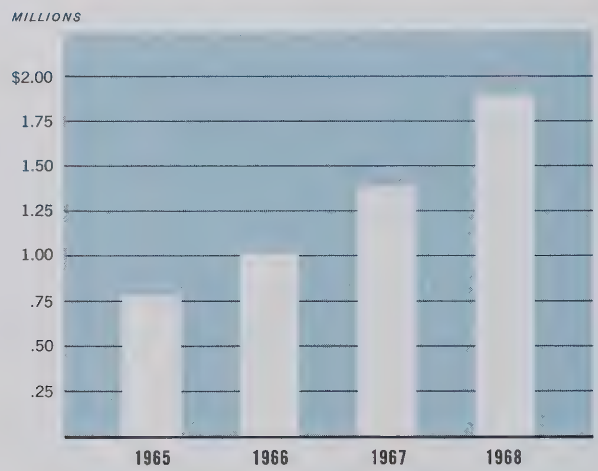
T. B. PICKENS, JR.
President

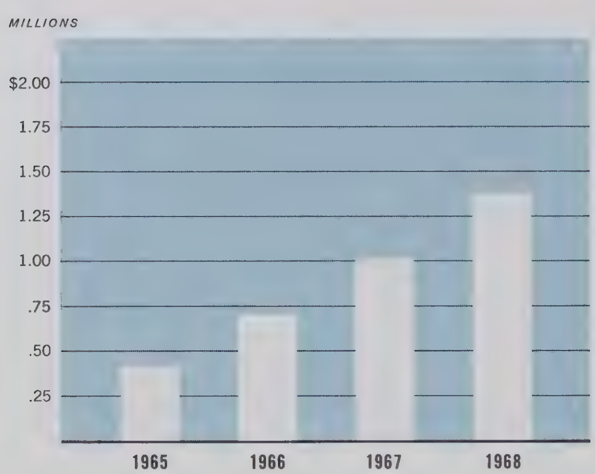
Date July 25, 1968



GROSS REVENUE

CASH FLOW





NET INCOME

Summary OF OPERATIONS

MESA
PETROLEUM CO.

At year end, Mesa's undeveloped oil and gas leases, permits, reservations and concessions not held by production covered approximately 3.8 million gross acres and represents a cost to the Company of about $2.9 million. The table below reflects Mesa's undeveloped gross and net acreage position by areas.

Area	*Gross Acres*	*Net Acres*
Alberta*	347,274	201,485
British Columbia*	180,318	47,319
Manitoba*	842,949	70,392
Northwest Territories*	1,021,483	1,021,483
Ontario	43,211	4,321
Saskatchewan*	235,672	209,448
Alaska	20,413	15,309
California	11,520	101
Colorado	10,117	10,117
Kansas	3,913	3,273
Montana	173,970	116,766
Oklahoma	25,293	17,562
Texas	1,971	1,971
Wyoming	10,311	9,249
Republic of Austria (concession)	879,000	879,000
Total	3,807,415	2,607,796

* Includes drilling reservations, petroleum and natural gas reservations, permits and leases.

Mesa participated in the drilling of 74 wells during the fiscal year ended April 30, 1968. The following table summarizes our drilling activities and results during the past two years:

	1968		*1967*	
	Gross	*Net*	*Gross*	*Net*
Oil	18	5.4	18	8.2
Gas	11	2.5	17	3.9
Dry	45	12.4	42	11.3
	74	20.3	77	23.4

On April 30, 1968 Mesa held interests in 247 producing wells — 93 gas and 154 oil. This is equivalent to 24.2 net gas wells and 71.3 net oil wells or a total of 95.5 net wells.

Mesa's oil and gas production during fiscal 1968 reached record highs. The Company's share of oil and condensate production totaled 329,000 barrels and its share of gas production amounted to nearly 3.7 billion cubic feet. This is an increase of 30% and 16%, respectively, over fiscal 1967.

Production for the next year will show additional increases as the 16 gross shut-in gas wells are connected to transmission lines. Mesa successfully completed discovery wells at West Trail, Dewey County, Oklahoma, No Water Creek, Washakie County, Wyoming, and Moose Lick, British Columbia. The Company also has an indicated discovery at Altares in British Columbia. Several development wells near these discoveries will be drilled during the coming year.

Consolidated Statements of Income

For The Years Ended April 30

	1968	1967
REVENUES:		
Oil and gas sales	$1,248,278	$1,022,865
Proceeds from drilling arrangements and sales of oil and gas leases held for resale	4,494,652	3,836,840
Gilsonite sales and other income	444,895	409,103
	$6,187,825	$5,268,808
CASH EXPENSES:		
Lease operating expenses	$ 321,660	$ 255,485
Cost of drilling arrangements and sales of oil and gas leases held for resale	2,859,585	2,555,367
Cost of gilsonite sales and other operating expenses	366,135	385,060
General and administrative	606,176	480,876
Interest	135,159	194,903
	$4,288,715	$3,871,691
Income from operations before depreciation, depletion and amortization	$1,899,110	$1,397,117
DEPRECIATION, DEPLETION AND AMORTIZATION (Note 2)	509,355	389,447
Net income (Note 3)	$1,389,755	$1,007,670
Net income per share based on average shares outstanding (Note 6)	$1.98	$1.56

(See accompanying notes to financial statements.)

Consolidated Statements of Source and Use of Funds

For The Years Ended April 30

	1968	1967
Funds Were Obtained From:		
Cash income from operations	$1,899,110	$1,397,117
Long-term loans less repayments	1,615,925	631,820
Disposals of property, plant and equipment	—	935,000
Net proceeds from sale of Convertible Debentures	3,763,222	—
Proceeds from exercise of stock options	16,057	—
	$7,294,314	$2,963,937
Funds Were Used For:		
Capital expenditures — net of retirements	$3,440,527	$2,381,152
Reduction of deferred income from sale of production payment	170,505	159,390
Payment of cash dividends	58,574	53,200
Increase in investments and other assets	492,351	32,755
Increase in working capital	3,132,357	337,440
	$7,294,314	$2,963,937

(See accompanying notes to financial statements.)

MESA PETROLEUM CO.

Consolidated Balanc

	1968	1967
Current Assets:		
Cash	$ 552,818	$ 422,343
Accounts receivable:		
Oil and gas operations	2,235,801	649,466
Other	67,691	85,075
Inventories, at cost:		
Oil and gas leases held for resale within one year	1,234,924	485,205
Gilsonite products	37,548	32,021
Prepaid expenses	33,453	18,155
Total current assets	$ 4,162,235	$1,692,265
Investments, at cost	$ 572,341	$ 141,305
Property, Plant and Equipment, at cost (partially pledged to secure long-term debt) Note 2:		
Producing and nonproducing oil and gas leases, wells and equipment	$ 9,694,092	$6,312,945
Gilsonite mining properties, plant and equipment	1,155,870	1,153,465
Automotive, office and other properties	357,936	328,305
	$11,207,898	$7,794,715
Less — Accumulated depreciation, depletion and amortization	1,591,926	1,109,915
	$ 9,615,972	$6,684,800
Deferred Charges and Other Assets	$ 175,465	$ 114,150
	$14,526,013	$8,632,520

(See accompanying notes to financial statements.)

Sheets APRIL 30, 1968 AND 1967

MESA PETROLEUM CO.

	1968	1967
CURRENT LIABILITIES:		
Current maturities on long-term debt	$ 11,500	$ 470,846
Short-term bank loans payable	—	142,940
Accounts payable and accrued liabilities	804,598	882,251
Royalties payable	121,163	103,611
Total current liabilities	$ 937,261	$1,599,648
LONG-TERM DEBT, net of current maturities (Note 4)	$ 3,880,465	$2,264,540
DEFERRED INCOME FROM SALE OF PRODUCTION PAYMENT (Note 5)	$ 220,105	$ 390,610
STOCKHOLDERS' INVESTMENT (Notes 6 and 7):		
Preferred stock, $1 par value, authorized 1,000,000 shares; none issued		
Common stock, $1 par value, authorized 5,000,000 shares; issued 798,659 shares in 1968 and 586,507 shares in 1967	$ 798,659	$ 586,507
Capital surplus	7,085,982	1,784,115
Reinvested earnings	1,603,541	2,027,670
	$ 9,488,182	$4,398,292
Less — Treasury stock, 1,316 shares, at cost	—	20,570
	$ 9,488,182	$4,377,722
	$14,526,013	$8,632,520

(See accompanying notes to financial statements.)

Consolidated Statements of Reinvested Earnings and Capital Surplus

MESA PETROLEUM CO.

For The Years Ended April 30

Reinvested Earnings

	1968	1967
Balance, beginning of year	$2,027,670	$1,073,200
Net income for the year	1,389,755	1,007,670
Dividends paid — Cash	(58,574)	(53,200)
Stock	(1,755,310)	—
Balance, end of year	$1,603,541	$2,027,670

Capital Surplus

	1968	1967
Balance, beginning of year	$1,784,115	$1,837,314
Excess market value over par value of 10% stock dividend	1,696,308	—
Transfer to capital stock on stock split, effected in the form of a stock dividend	—	(53,199)
Excess of conversion amount over par value of 152,817 shares of common stock issued in connection with the conversion of $3,979,000 of 5¾% Convertible Subordinated Debentures due 1982, less unamortized bond issuance costs of $215,779 (Note 6)	3,610,404	—
Excess cost over proceeds received from sale of treasury stock to officers and key employees under stock option plan	(4,845)	—
Balance, end of year	$7,085,982	$1,784,115

(See accompanying notes to financial statements)

Notes to Consolidated Financial Statements

April 30, 1968

(1) Principles of Consolidation:

The consolidated financial statements include the accounts of the parent, Mesa Petroleum Co., and its five totally held subsidiaries. All significant intercompany transactions have been eliminated. Conversion from foreign currency, where necessary, was made in accordance with generally accepted accounting principles and differences resulting from exchange fluctuations are insignificant.

(2) Accounting Policy Relating to Oil and Gas Properties and Depreciation:

The Company follows the accounting policy of capitalizing, for financial reporting purposes, all direct costs incurred in the acquisition, exploration, and development of gas and oil reserves, including nonproductive costs. Such capitalized costs are being amortized on a company-wide composite unit-of-production method over the aggregate productive life of all of its producing properties. Under this method of accounting, no gains or losses are recognized upon the sale or disposition of oil and gas properties, except in extraordinary transactions. Through April 30, 1968, nonproductive costs capitalized, net of gains on sales of producing properties which have been credited to property and amortization, amounted to approximately $1,475,000.

(3) Federal Income Taxes:

Because of the deductibility for tax purposes of amounts capitalized and amortized for financial reporting purposes, no provision for Federal or Canadian income taxes for the year ended April 30, 1968, has been necessary. To date, the Company has received no Federal income tax benefits from nonproductive well costs capitalized for financial reporting purposes.

As of April 30, 1968, the Company has estimated unused operating loss carry-forwards of $1,400,000 which are available to reduce or eliminate Federal income taxes which may be payable in future periods. These losses, if not utilized, will expire by 1973.

(4) Long-Term Debt:

On March 15, 1968, the Company entered into a revolving credit agreement with a bank under which it may borrow up to $3,860,000 at any time before May 15, 1969, at an interest rate of 6¾%. The bank has also agreed to make a term loan to the Company at May 15, 1969 in an amount not to exceed $3,860,000. The loan would be repayable in sixty-six monthly installments and bear interest at ¾ of 1 percent above the then prime rate or 6¾%, whichever is greater. The loan agreement contains certain provisions and restrictions pertaining to dividend payments, working capital, net worth, capital expenditures and other matters. Should the Debentures to be offered under a Registration Statement filed with the Securities and Exchange Commission on June 24, 1968 be sold, a portion of the proceeds will be applied to the complete liquidation of this loan, in which event, the bank's obligation to make further revolving credit advances after such liquidation and a term loan to the Company at May 15, 1969 will be renegotiated.

Long-term debt and other obligations at April 30, 1968, consisted of the following:

	Long-Term	*Current*	*Total*
6¾% revolving credit note payable to a bank secured by mortgages on substantially all producing oil and gas properties	$3,860,000	$ —	$3,860,000
Noninterest-bearing purchase obligation, payable at the rate of $2 per ton of ore removed from certain gilsonite properties	19,965	11,000	30,965
Other	500	500	1,000
	$3,880,465	$ 11,500	$3,891,965

Notes to Consolidated Financial Statements

(CONTINUED)

MESA PETROLEUM CO.

(5) SALE OF PRODUCTION PAYMENT:

In April, 1966, the Company sold interests in future production (production payment) from certain of its oil and gas properties for $550,000. The principal amount, plus an amount equivalent to interest of 6¾% on the unpaid balance, is payable out of 80 percent of the company's share in production from the properties. The proceeds from the sale have been deferred for financial reporting purposes and are being taken into income as the oil and gas are produced.

(6) CAPITAL STOCK AND SALE OF CONVERTIBLE DEBENTURES:

In September, 1967, the stockholders approved an increase from 1,000,000 to 5,000,000 the number of authorized shares of common stock. At the same time, the stockholders also authorized a new class of preferred stock consisting of 1,000,000 shares with a par value of $1. Through April 30, 1968, no preferred shares had been issued.

On August 2, 1967, the Company sold $4,000,000 principal amount of Convertible Subordinated Debentures due 1982. The Debentures were convertible at the options of the holder into common stock of the Company at the rate of $25.91 principal amount of debentures per share.

On January 12, 1968, the Company called for redemption the Convertible Debentures and the holders thereof exercised their option and exchanged $3,979,000 principal amount of Debentures for 152,817 shares of common stock. The remaining $21,000 of Debentures were redeemed by the Company.

Pro forma net income per share assuming that the debentures had been converted on the date issued would have been $1.83.

(7) STOCK OPTIONS:

Under a qualified stock option plan approved by the stockholders in 1965, 34,651 shares of authorized and unissued common stock are reserved for options which may be granted to officers and key employees at prices equivalent to market value on the date of grant. The options become exercisable in four annual installments commencing one year after the date granted and if not exercised, expire five years after the date of grant. As of April 30, 1968, options for 10,983 shares were outstanding at prices ranging from $8.89 to $36.63 per share or a total value of $149,051. During the year ended April 30, 1968, options for 1,649 shares have been exercised at per share prices ranging from $8.89 to $19.09 for an aggregate option value of $16,057 (market value of $56,478). Upon exercising of options the company credits the capital stock account with the par value of the shares purchased and credits the balance of the cash received to capital surplus and no charge is made to income.

Auditors' Report

TO MESA PETROLEUM CO.

We have examined the consolidated balance sheet of Mesa Petroleum Co. (a Delaware corporation) and subsidiaries as of April 30, 1968, and the related consolidated statements of income, reinvested earnings, capital surplus and source and use of funds for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements set forth above present fairly the financial position of Mesa Petroleum Co. and subsidiaries as of April 30, 1968, and the results of their operations and their source and use of funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

ARTHUR ANDERSEN & CO.

Houston, Texas
June 5, 1968

DIRECTORS

LAWTON L. CLARK
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WALES H. MADDEN, JR.*
DON S. MARSALIS
JOHN G. O'BRIEN
T. B. PICKENS, JR.*
HOWARD F. SAUNDERS
E. H. SELECMAN
RICHARD S. SMITH
HOLLAND E. TOLES
THOMAS R. YOUNG

OFFICERS

T. B. PICKENS, JR., *President and Chairman of the Board of Directors*
LAWTON L. CLARK, *Vice President*
FRANK W. PODPECHAN, *Vice President*
JOHN F. BOROS, *Secretary and Treasurer*

* Member of Executive Committee

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